
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended **March 31, 2016**

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**



Pacific Ethanol, Inc.

(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 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 period that the registrant was required to submit and post such files). Yes 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

Non-accelerated filer (Do not check if a smaller reporting company)

Accelerated filer

Smaller reporting company

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

As of May 9, 2016, there were 39,273,248 shares of Pacific Ethanol, Inc. common stock, \$0.001 par value per share, and 3,540,132 shares of Pacific Ethanol, Inc. non-voting common stock, \$0.001 par value per share, outstanding.

	<u>Page</u>
<u>PART I - FINANCIAL INFORMATION</u>	
ITEM 1. <u>FINANCIAL STATEMENTS</u>	3
<u>Consolidated Balance Sheets as of March 31, 2016 (unaudited) and December 31, 2015</u>	3
<u>Consolidated Statements of Operations for the Three Months Ended March 31, 2016 and 2015 (unaudited)</u>	5
<u>Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2016 and 2015 (unaudited)</u>	6
<u>Notes to Consolidated Financial Statements (unaudited)</u>	7
ITEM 2. <u>MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	18
ITEM 3. <u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	29
ITEM 4. <u>CONTROLS AND PROCEDURES</u>	30
<u>PART II - OTHER INFORMATION</u>	
ITEM 1. <u>LEGAL PROCEEDINGS</u>	31
ITEM 1A. <u>RISK FACTORS</u>	31
ITEM 2. <u>UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS</u>	42
ITEM 3. <u>DEFAULTS UPON SENIOR SECURITIES</u>	42
ITEM 4. <u>MINE SAFETY DISCLOSURES</u>	42
ITEM 5. <u>OTHER INFORMATION</u>	42
ITEM 6. <u>EXHIBITS</u>	43
<u>SIGNATURES</u>	44

PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

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

	March 31, 2016 (unaudited)	December 31, 2015 *
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 19,207	\$ 52,712
Accounts receivable, net (net of allowance for doubtful accounts of \$281 and \$25, respectively)	63,414	61,346
Inventories	69,262	60,820
Prepaid inventory	6,008	5,973
Income tax receivables	6,120	10,654
Other current assets	6,222	6,437
Total current assets	<u>170,233</u>	<u>197,942</u>
Property and equipment, net	<u>461,275</u>	<u>464,960</u>
Other Assets:		
Intangible assets, net	2,678	2,678
Other assets	9,013	9,100
Total other assets	<u>11,691</u>	<u>11,778</u>
Total Assets	<u>\$ 643,199</u>	<u>\$ 674,680</u>

* Amounts derived from the audited financial statements for the year ended December 31, 2015.

See accompanying notes to consolidated financial statements.

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

	March 31, 2016 (unaudited)	December 31, 2015 *
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable – trade	\$ 27,080	\$ 30,520
Accrued liabilities	15,016	10,072
Current portion – capital leases	4,338	4,248
Current portion – long-term debt	—	17,003
Accrued PE Op Co. purchase	3,828	3,828
Other current liabilities	7,294	7,238
Total current liabilities	57,556	72,909
Long-term debt, net of current portion	202,973	203,861
Capital leases, net of current portion	3,064	4,183
Warrant liabilities at fair value	234	273
Deferred tax liabilities	1,174	1,174
Other liabilities	19,614	20,736
Total Liabilities	284,615	303,136
Commitments and Contingencies (Note 6)		
Stockholders' Equity:		
Pacific Ethanol, Inc. Stockholders' Equity:		
Preferred stock, \$0.001 par value; 10,000,000 shares authorized; Series A: 1,684,375 shares authorized; no shares issued and outstanding as of March 31, 2016 and December 31, 2015; Series B: 1,580,790 shares authorized; 926,942 shares issued and outstanding as of March 31, 2016 and December 31, 2015; liquidation preference of \$18,075 as of March 31, 2016	1	1
Common stock, \$0.001 par value; 300,000,000 shares authorized; 39,351,765 and 38,974,972 shares issued and outstanding as of March 31, 2016 and December 31, 2015, respectively	39	39
Non-voting common stock, \$0.001 par value; 3,553,000 shares authorized; 3,540,132 shares issued and outstanding as of March 31, 2016 and December 31, 2015	4	4
Additional paid-in capital	903,424	902,843
Accumulated other comprehensive income	1,040	1,040
Accumulated deficit	(545,924)	(532,383)
Total Stockholders' Equity	358,584	371,544
Total Liabilities and Stockholders' Equity	\$ 643,199	\$ 674,680

* Amounts derived from the audited financial statements for the year ended December 31, 2015.

See accompanying notes to consolidated financial statements.

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

	Three Months Ended March 31,	
	2016	2015
Net sales	\$ 342,373	\$ 206,176
Cost of goods sold	341,304	207,163
Gross profit (loss)	1,069	(987)
Selling, general and administrative expenses	8,317	4,905
Loss from operations	(7,248)	(5,892)
Fair value adjustments	39	(173)
Interest expense, net	(6,233)	(1,015)
Other income (expense), net	216	(129)
Loss before provision for income taxes	(13,226)	(7,209)
Benefit for income taxes	—	2,700
Consolidated net loss	(13,226)	(4,509)
Net loss attributed to noncontrolling interests	—	129
Net loss attributed to Pacific Ethanol, Inc.	\$ (13,226)	\$ (4,380)
Preferred stock dividends	\$ (315)	\$ (312)
Net loss attributed to common stockholders	\$ (13,541)	\$ (4,692)
Net loss per share, basic and diluted	\$ (0.32)	\$ (0.19)
Weighted-average shares outstanding, basic and diluted	42,052	24,104

See accompanying notes to consolidated financial statements.

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

	Three Months Ended March 31,	
	2016	2015
Operating Activities:		
Consolidated net loss	\$ (13,226)	\$ (4,509)
Adjustments to reconcile consolidated net loss to net cash provided by (used in) operating activities:		
Fair value adjustments	(39)	173
Depreciation and amortization of intangibles	8,651	3,409
Interest expense added to term debt	3,786	—
Amortization of debt discount	301	44
Non-cash compensation	583	506
Amortization of deferred financing fees	54	60
Loss (gain) on derivatives	(582)	189
Bad debt expense	256	—
Changes in operating assets and liabilities:		
Accounts receivable	(2,324)	7,270
Inventories	(8,442)	709
Prepaid expenses and other assets	5,439	(2,857)
Prepaid inventory	(35)	3,164
Accounts payable and accrued expenses	416	(832)
Net cash provided by (used in) operating activities	<u>(5,162)</u>	<u>7,326</u>
Investing Activities:		
Additions to property and equipment	(4,966)	(8,178)
Net cash used in investing activities	<u>(4,966)</u>	<u>(8,178)</u>
Financing Activities:		
Net payments on Kinery's line of credit	(5,031)	(17,530)
Principal payments on borrowings	(17,003)	—
Principal payments on capital leases	(1,028)	(1,307)
Proceeds from exercise of warrants	—	191
Preferred stock dividends paid	(315)	(312)
Net cash used in financing activities	<u>(23,377)</u>	<u>(18,958)</u>
Net decrease in cash and cash equivalents	(33,505)	(19,810)
Cash and cash equivalents at beginning of period	52,712	62,084
Cash and cash equivalents at end of period	<u>\$ 19,207</u>	<u>\$ 42,274</u>
Supplemental Information:		
Interest paid	\$ 2,070	\$ 969
Income taxes received	<u>\$ 4,534</u>	<u>\$ —</u>

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, for all periods presented, the accounts of Pacific Ethanol, Inc., a Delaware corporation (“Pacific Ethanol”), and its direct and indirect subsidiaries (collectively, the “Company”), including its wholly-owned subsidiaries, Kinergy Marketing LLC, an Oregon limited liability company (“Kinergy”), Pacific Ag. Products, LLC, a California limited liability company (“PAP”) and PE Op Co., a Delaware corporation (“PE Op Co.”).

The Company’s acquisition of Aventine Renewable Energy Holdings, Inc. (now, Pacific Ethanol Central, LLC, a Delaware limited liability company, “Aventine”) was consummated on July 1, 2015, and as a result, the Company’s consolidated financial statements include the results of Aventine only as of and for the three months ended March 31, 2016.

The Company is a leading producer and marketer of low-carbon renewable fuels in the United States. The Company’s four ethanol plants in the Western United States (together with their respective holding companies, the “Pacific Ethanol West Plants”) are located in close proximity to both feed and ethanol customers and thus enjoy unique advantages in efficiency, logistics and product pricing. These plants produce among the lowest-carbon ethanol produced in the United States due to low energy use in production.

With the addition of four Midwestern ethanol plants in July 2015 as a result of the Company’s acquisition of Aventine, the Company now has a combined ethanol production capacity of 515 million gallons per year, markets, on an annualized basis, over 800 million gallons of ethanol, and produces, on an annualized basis, over one million tons of co-products such as wet and dry distillers grains, wet and dry corn gluten feed, condensed distillers solubles, corn gluten meal, corn germ, distillers yeast and CO₂. The Company’s four ethanol plants in the Midwest (together with their respective holding companies, the “Pacific Ethanol Central Plants”) are located in the heart of the Corn Belt, benefit from low-cost and abundant feedstock production and allow for access to many additional domestic markets. In addition, the Company’s ability to load unit trains from these facilities in the Midwest allows for greater access to international markets.

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, sells distillers grains and other feed co-products to dairy operators and animal feedlots and sells corn oil to poultry and biodiesel customers 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 \$44,233,000 and \$42,049,000 at March 31, 2016 and December 31, 2015, respectively, were used as collateral under Kinergy's operating line of credit. The allowance for doubtful accounts was \$281,000 and \$25,000 as of March 31, 2016 and December 31, 2015, respectively. The Company recorded a bad debt expense of \$256,000 and none for the three months ended March 31, 2016 and 2015, respectively. The Company does not have any off-balance sheet credit exposure related to its customers.

Benefit for Income Taxes – The Company recognized none and \$2.7 million in tax benefit for the three months ended March 31, 2016 and 2015, respectively, related to losses incurred to the extent they were able to be carried back to a prior taxable year. For the three months ended March 31, 2016, the Company applied a valuation allowance against the amount of deferred tax losses from the period. To the extent the Company believes it can utilize these losses, it will adjust its provision (benefit) for income taxes accordingly in future periods.

Financial Instruments – The carrying values of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities are reasonable estimates of their fair values because of the short maturity of these items. The Company recorded its warrants at fair value. The Company believes the carrying value of its long-term debt approximates fair value because the interest rates on these instruments are variable.

Reclassifications – Certain prior year amounts have been reclassified to conform to the current presentation. Such reclassification had no effect on the consolidated net loss reported in the consolidated statements of operations.

Recent Accounting Pronouncements – In February 2016, the Financial Accounting Standards Board (“FASB”) issued new guidance on accounting for leases. Under the new guidance, lessees will be required to recognize the following for all leases (with the exception of short-term leases) at the commencement date: (1) a lease liability, which is a lessee's obligation to make lease payments arising from a lease, measured on a discounted cash flow basis; and (2) a “right of use” asset, which is an asset that represents the lessee's right to use the specified asset for the lease term. Under the new guidance, lessor accounting is largely unchanged, with some minor exceptions. Lessees will no longer be provided with a source of off-balance sheet financing for other than short-term leases. The standard is effective for public companies for annual reporting periods beginning after December 15, 2019, and for interim periods beginning after December 15, 2020. Early adoption is permitted. The Company has several operating leases that may be impacted by this guidance. The Company is currently evaluating the impact of the adoption of this accounting standard on its consolidated results of operations and financial condition.

In May 2014, the FASB issued new guidance on the recognition of revenue. The guidance states that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The standard was originally effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period, but has been further deferred one year. The Company's adoption begins with the first fiscal quarter of fiscal year 2018. In March and April 2016, the FASB issued further revenue recognition guidance amending principal vs. agent considerations whether an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods and services. The Company is currently evaluating the impact of the adoption of this accounting standard update on its consolidated results of operations and financial condition.

In September 2015, the FASB issued new guidance on simplifying the accounting for measurement-period adjustments. Under the new guidance, an acquirer must recognize adjustments to provisional amounts that are identified during the measurement period in the reporting period in which the adjustment amounts are determined. The guidance also requires acquirers to present separately on the face of the statement of operations or disclose in the notes, the portion of the amount recorded in current-period earnings by line item that would have been recorded in previous reporting periods if the adjustment to the provisional amounts had been recognized as of the acquisition date. The guidance is effective for fiscal years beginning after December 31, 2015, applied prospectively. Early adoption is permitted. The Company will consider early adoption in future periods related to its current measurement period for its acquisition of Aventine.

In April 2015, the FASB issued new guidance on presentation of debt issuance costs. Historically, entities have presented debt issuance costs as an asset. Under the new guidance, effective for fiscal years beginning after December 31, 2015, debt issuance costs have been reclassified as a deduction to the carrying amount of the related debt balance. The guidance does not change any of the Company's other debt recognition or disclosure. The Company adopted this guidance beginning January 1, 2016.

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, 2015. 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, 2015. 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 the fair value of warrants, allowance for doubtful accounts, net realized value of inventory, 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.

2. SEGMENTS.

The Company reports its financial and operating performance in two segments: (1) ethanol production, which includes the production and sale of ethanol and co-products, with all eight of the Company's production facilities aggregated, and (2) marketing and distribution, which includes marketing and merchant trading for Company-produced ethanol and co-products and third-party ethanol.

The following tables set forth certain financial data for the Company's operating segments (in thousands):

	Three Months Ended March 31,	
	2016	2015
<u>Net Sales:</u>		
Ethanol production:		
Net sales from external customers	\$ 229,241	\$ 98,997
Intersegment net sales	—	—
Total segment revenues	<u>229,241</u>	<u>98,997</u>
Marketing and distribution:		
Net sales from external customers	113,132	107,179
Intersegment net sales	2,016	735
Total segment net sales	<u>115,148</u>	<u>107,914</u>
Net sales including intersegment activity	344,389	206,911
Intersegment eliminations	<u>(2,016)</u>	<u>(735)</u>
Net sales as reported	<u>\$ 342,373</u>	<u>\$ 206,176</u>
<u>Cost of goods sold:</u>		
Ethanol production	\$ 236,008	\$ 101,537
Marketing and distribution	109,297	108,059
Intersegment eliminations	<u>(4,001)</u>	<u>(2,433)</u>
	<u>\$ 341,304</u>	<u>\$ 207,163</u>
<u>Income (loss) before provision for income taxes:</u>		
Ethanol production	\$ (17,322)	\$ (5,360)
Marketing and distribution	3,969	(1,615)
Corporate activities	127	(234)
	<u>\$ (13,226)</u>	<u>\$ (7,209)</u>
<u>Depreciation and amortization:</u>		
Ethanol production	\$ 8,415	\$ 3,184
Marketing and distribution	3	127
Corporate activities	<u>233</u>	<u>98</u>
	<u>\$ 8,651</u>	<u>\$ 3,409</u>
<u>Interest expense:</u>		
Ethanol production	\$ (5,900)	\$ (922)
Marketing and distribution	(333)	(93)
Corporate activities	—	—
	<u>\$ (6,233)</u>	<u>\$ (1,015)</u>

The following table sets forth the Company's total assets by operating segment (in thousands):

	March 31, 2016	December 31, 2015
<u>Total assets:</u>		
Ethanol production	\$ 521,977	\$ 536,013
Marketing and distribution	106,137	107,069
Corporate assets	15,085	31,598
	<u>\$ 643,199</u>	<u>\$ 674,680</u>

3. INVENTORIES.

Inventories consisted primarily of bulk ethanol, corn, co-products, Low-Carbon Fuel Standard (“LCFS”) credits and unleaded fuel, and are valued at the lower-of-cost-or-net realizable value, with cost determined on a first-in, first-out basis. Inventory balances consisted of the following (in thousands):

	<u>March 31, 2016</u>	<u>December 31, 2015</u>
Finished goods	\$ 34,278	\$ 31,153
LCFS credits	16,856	6,957
Raw materials	8,136	9,891
Work in progress	8,338	11,121
Other	1,654	1,698
Total	<u>\$ 69,262</u>	<u>\$ 60,820</u>

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. 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 months ended March 31, 2016 and 2015, 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 exchange-traded 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 gains of \$582,000 and losses of \$189,000 as the change in the fair value of these contracts for the three months ended March 31, 2016 and 2015, respectively.

Non Designated Derivative Instruments – The classification and amounts of the Company’s derivatives not designated as hedging instruments are as follows (in thousands):

As of March 31, 2016				
Type of Instrument	Assets		Liabilities	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity contracts	Other current assets	\$ 1,774	Other current liabilities	\$ 1,868
		\$ 1,774		\$ 1,868

As of December 31, 2015				
Type of Instrument	Assets		Liabilities	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Commodity contracts	Other current assets	\$ 2,081	Other current liabilities	\$ 1,848
		\$ 2,081		\$ 1,848

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

Type of Instrument	Statements of Operations Location	Realized Gains (Losses) Three Months Ended March 31,	
		2016	2015
Commodity contracts	Cost of goods sold	\$ 908	\$ (115)

Type of Instrument	Statements of Operations Location	Unrealized Losses Three Months Ended March 31,	
		2016	2015
Commodity contracts	Cost of goods sold	\$ (326)	\$ (74)

5. DEBT.

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

	March 31, 2016	December 31, 2015
Kinergy operating line of credit	\$ 55,972	\$ 61,003
Term debt	149,405	162,622
	205,377	223,625
Less unamortized discount	(1,996)	(2,299)
Less unamortized debt financing costs	(408)	(462)
Less short-term portion	—	(17,003)
Long-term debt	\$ 202,973	\$ 203,861

Kinergy Operating Line of Credit – As of March 31, 2016, Kinergy had an available borrowing base under its credit facility of \$7,366,000.

Plant Term Debt – On February 26, 2016, the Company retired the \$17,003,000 outstanding balance of the Pacific Ethanol West Plants’ term debt by purchasing the lender’s position for cash at par without any prepayment penalty. The purchase increased the amount of the term debt held by Pacific Ethanol to a combined \$58,766,000, which is eliminated upon consolidation. As a result, the Company has no continuing obligations to any third-party lender under the credit agreements associated with the Pacific Ethanol West Plants’ term debt.

For the three months ended March 31, 2016, the Pacific Ethanol Central Plants elected to defer interest payments on their term debt in the aggregate amount of \$3,786,000, which was added to the outstanding term debt balance.

At March 31, 2016, there were approximately \$145.0 million of net assets of the Company’s subsidiaries that were not available to be transferred to the parent company in the form of dividends, loans or advances due to restrictions contained in the credit facilities of these subsidiaries.

6. COMMITMENTS AND CONTINGENCIES.

Sales Commitments – At March 31, 2016, the Company had entered into sales contracts with its major customers to sell certain quantities of ethanol and co-products. The Company had open ethanol indexed-price ethanol sales contracts for 311,013,000 gallons as of March 31, 2016 and open fixed-price ethanol sales contracts valued at \$7,175,000 as of March 31, 2016. The Company had open fixed-price co-product sales contracts valued at \$33,500,000 and open indexed-price co-product sales contracts for 145,000 tons as of March 31, 2016. These sales contracts are scheduled to be completed throughout 2016.

Purchase Commitments – At March 31, 2016, the Company had indexed-price purchase contracts to purchase 30,835,000 gallons of ethanol and fixed-price purchase contracts to purchase \$10,326,000 of ethanol from its suppliers. The Company had fixed-price purchase contracts to purchase \$20,500,000 of corn from its suppliers. These purchase commitments are scheduled to be satisfied throughout 2016.

Litigation – General – The Company is subject to various claims and contingencies in the ordinary course of its business, including those related to litigation, business transactions, employee-related matters, and others. When the Company is aware of a claim or potential claim, it assesses the likelihood of any loss or exposure. If it is probable that a loss will result and the amount of the loss can be reasonably estimated, the Company will record a liability for the loss. If the loss is not probable or the amount of the loss cannot be reasonably estimated, the Company discloses the claim if the likelihood of a potential loss is reasonably possible and the amount involved could be material. While there can be no assurances, the Company does not expect that any of its pending legal proceedings will have a material financial impact on the Company’s operating results.

Pacific Ethanol, Inc., through a subsidiary acquired in its acquisition of Aventine, became involved in a pending lawsuit with Western Sugar Cooperative (“Western Sugar”) that pre-dated the Aventine acquisition.

On February 27, 2015, Western Sugar filed a complaint in the United States District Court for the District of Colorado (Case No. 1:15-cv-00415) naming Aventine Renewable Energy, Inc. (“ARE, Inc.”), one of Aventine’s subsidiaries, as defendant. Western Sugar amended its complaint on April 21, 2015. ARE, Inc. purchased surplus sugar through a United States Department of Agriculture program. Western Sugar was one of the entities that warehoused this sugar for ARE, Inc. The suit alleges that ARE, Inc. breached its contract with Western Sugar by failing to pay certain penalty rates for the storage of its sugar or alternatively failing to pay a premium rate for storage. Western Sugar alleges that the penalty rates apply because ARE, Inc. failed to take timely delivery or otherwise cause timely shipment of the sugar. Western Sugar claims “expectation damages” in the amount of approximately \$8.6 million. ARE, Inc. filed answers to Western Sugar’s complaint and amended complaint generally denying Western Sugar’s allegations and asserting various defenses. The case is currently in its discovery phase.

The Company has evaluated the above case as well as other pending cases. The Company currently has recorded \$3.3 million as a litigation contingency liability with respect to these cases for amounts that are probable and estimable.

7. PENSION AND RETIREMENT BENEFIT PLANS.

The Company, through its acquisition of Aventine, has assumed a defined benefit pension plan (the “Pension Plan”) and a health care and life insurance plan (the “Postretirement Plan”).

The Pension Plan is noncontributory, and covers unionized employees at the Company’s Pekin, Illinois facility, who fulfill minimum age and service requirements. Benefits are based on a prescribed formula based upon the employee’s years of service. The Pension Plan, part of a collective bargaining agreement, covers only Union employees hired after November 1, 2010. The Company uses a December 31 measurement date for its Pension Plan. The Company’s funding policy is to make the minimum annual contributions that are required by applicable regulations. As of December 31, 2015, the Pension Plan’s accumulated projected benefit obligation was \$16.6 million, with a fair value of plan assets of \$12.6 million. The underfunded amount of \$4.0 million is recorded on the Company’s consolidated balance sheet in other noncurrent liabilities. For the three months ended March 31, 2016, the Pension Plan’s net periodic expense was \$29,000, comprised of \$172,000 in interest cost and \$56,000 in service cost, partially offset by \$199,000 of expected return on plan assets.

The Postretirement Plan provides postretirement medical benefits and life insurance to certain “grandfathered” unionized employees. Employees hired after December 31, 2000 are not eligible to participate in the Postretirement Plan. The Postretirement Plan is contributory, with contributions required at the same rate as active employees. Benefit eligibility under the plan reduces at age 65 from a defined benefit to a defined collar cap based upon years of service. As of December 31, 2015, the Postretirement Plan’s accumulated projected benefit obligation was \$3.6 million and is recorded on the Company’s consolidated balance sheet in other noncurrent liabilities. The Company’s funding policy is to make the minimum annual contributions that are required by applicable regulations. For the three months ended March 31, 2016, the Postretirement Plan’s net periodic expense was \$47,000, comprised of \$35,000 of interest cost and \$12,000 of service cost.

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.

The Company recorded its warrants issued from 2010 through 2013 at fair value and designated them as Level 3 on their issuance dates.

Warrants – The Company’s warrants were valued using a Monte Carlo Binomial Lattice-Based valuation methodology, adjusted for marketability restrictions.

Significant assumptions used and related fair values for the warrants as of March 31, 2016 were as follows:

<u>Original Issuance</u>	<u>Exercise Price</u>	<u>Volatility</u>	<u>Risk Free Interest Rate</u>	<u>Term (years)</u>	<u>Market Discount</u>	<u>Warrants Outstanding</u>	<u>Fair Value</u>
07/3/2012	\$ 6.09	51.1%	0.59%	1.26	22.1%	211,000	\$ 178,000
12/13/2011	\$ 8.43	52.9%	0.49%	0.70	17.4%	138,000	56,000
							<u>\$ 234,000</u>

Significant assumptions used and related fair values for the warrants as of December 31, 2015 were as follows:

<u>Original Issuance</u>	<u>Exercise Price</u>	<u>Volatility</u>	<u>Risk Free Interest Rate</u>	<u>Term (years)</u>	<u>Market Discount</u>	<u>Warrants Outstanding</u>	<u>Fair Value</u>
07/3/2012	\$ 6.09	49.1%	0.86%	1.51	22.9%	211,000	\$ 200,000
12/13/2011	\$ 8.43	48.4%	0.65%	0.95	18.3%	138,000	73,000
							<u>\$ 273,000</u>

The estimated fair value of the warrants is affected by the above underlying inputs. Observable inputs include the values of exercise price, stock price, term and risk-free interest rate. As separate inputs, an increase (decrease) in either the term or risk free interest rate will result in an increase (decrease) in the estimated fair value of the warrant.

Unobservable inputs include volatility and market discount. An increase (decrease) in volatility will result in an increase (decrease) in the estimated warrant value and an increase (decrease) in the market discount will result in a decrease (increase) in the estimated warrant fair value.

The volatility utilized was a blended average of the Company’s historical volatility and implied volatilities derived from a selected peer group. The implied volatility component has remained relatively constant over time given that implied volatility is a forward-looking assumption based on observable trades in public option markets. Should the Company’s historical volatility increase (decrease) on a go-forward basis, the resulting value of the warrants would increase (decrease).

The market discount, or a discount for lack of marketability, is quantified using a Black-Scholes option pricing model, with a primary model input of assumed holding period restriction. As the assumed holding period increases (decreases), the market discount increases (decreases), conversely impacting the value of the warrant fair value.

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

The following table summarizes recurring fair value measurements by level at March 31, 2016 (in thousands):

	Fair Value	Level 1	Level 2	Level 3
Assets:				
Derivative financial instruments(1)	\$ 1,774	\$ 1,774	\$ —	\$ —
	<u>\$ 1,774</u>	<u>\$ 1,774</u>	<u>\$ —</u>	<u>\$ —</u>
Liabilities:				
Warrants	\$ (234)	\$ —	\$ —	\$ (234)
Derivative financial instruments(4)	(1,868)	(1,868)	—	—
	<u>\$ (2,102)</u>	<u>\$ (1,868)</u>	<u>\$ —</u>	<u>\$ (234)</u>

The following table summarizes recurring fair value measurements by level at December 31, 2015 (in thousands):

	Fair Value	Level 1	Level 2	Level 3
Assets:				
Derivative financial instruments(1)	\$ 2,081	\$ 2,081	\$ —	\$ —
Defined benefit plan assets(2) (pooled separate accounts):				
Large U.S. Equity	3,662	—	3,662	—
Small/Mid U.S. Equity	1,099	—	1,099	—
International Equity	1,525	—	1,525	—
Fixed Income	6,281	—	6,281	—
	<u>\$ 14,648</u>	<u>\$ 2,081</u>	<u>\$ 12,567</u>	<u>\$ —</u>
Liabilities:				
Warrants (3)	\$ (273)	\$ —	\$ —	\$ (273)
Derivative financial instruments(4)	(1,848)	(1,848)	—	—
	<u>\$ (2,121)</u>	<u>\$ (1,848)</u>	<u>\$ —</u>	<u>\$ (273)</u>

(1) Included in other current assets in the consolidated balance sheets.

(2) Fair values of plan assets are determined annually and therefore are not included as of March 31, 2016. For further descriptions of these assets see the Company's Form 10-K for the year ended December 31, 2015.

(3) Included in warrant liabilities at fair value in the consolidated balance sheets.

(4) Included in accrued liabilities in the consolidated balance sheets.

For fair value measurements using significant unobservable inputs (Level 3), 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. The changes in the Company's fair value of its Level 3 inputs with respect to its warrants were as follows (in thousands):

Balance, December 31, 2015	\$ 273
Adjustments to fair value for the period	(39)
Balance, March 31, 2016	<u>\$ 234</u>

9. EARNINGS PER SHARE.

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

	Three Months Ended March 31, 2016		
	Shares		
	Loss Numerator	Denominator	Per-Share Amount
Net loss attributed to Pacific Ethanol, Inc.	\$ (13,226)		
Less: Preferred stock dividends	(315)		
Basic and diluted loss per share:			
Net loss attributed to common stockholders	<u>\$ (13,541)</u>	<u>42,052</u>	<u>\$ (0.32)</u>

	Three Months Ended March 31, 2015		
	Shares		
	Loss Numerator	Denominator	Per-Share Amount
Net loss attributed to Pacific Ethanol, Inc.	\$ (4,380)		
Less: Preferred stock dividends	(312)		
Basic and diluted loss per share:			
Net loss attributed to common stockholders	<u>\$ (4,692)</u>	<u>24,104</u>	<u>\$ (0.19)</u>

There were an aggregate of 635,000 and 1,080,000 potentially dilutive weighted-average shares from convertible securities outstanding as of March 31, 2016 and 2015, respectively. These convertible securities were not considered in calculating diluted net loss per share for the three months ended March 31, 2016 and 2015, as their effect would have been anti-dilutive.

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;
- fluctuations in the costs of key production input commodities such as corn and natural gas;
- 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;
- 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 below 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 a leading producer and marketer of low-carbon renewable fuels in the United States.

We own and operate eight strategically-located ethanol production facilities. Four of our plants are in the Western states of California, Oregon and Idaho, or the Pacific Ethanol West plants; and four of our plants are located in the Midwestern states of Illinois and Nebraska, or the Pacific Ethanol Central plants, acquired in our acquisition of Aventine Renewable Energy Holdings, Inc., or Aventine, on July 1, 2015. Our plants have a combined ethanol production capacity of 515 million gallons per year. We are the sixth largest producer of ethanol in the United States based on annualized volumes. We market all the ethanol and co-products produced at our eight plants as well as ethanol produced by third parties. On an annualized basis, we market over 800 million gallons of ethanol and over 1.5 million tons of ethanol co-products on a dry matter basis. Our business consists of two operating segments: a production segment and a marketing segment.

Our mission is to advance our position and significantly increase our market share as a leading producer and marketer of low-carbon renewable fuels in the United States. We intend to accomplish this goal in part by expanding our ethanol production capacity and distribution infrastructure, accretive acquisitions, lowering the carbon intensity of our ethanol, extending our marketing business into new regional and international markets, and implementing new technologies to promote higher production yields and greater efficiencies.

Production Segment

We produce ethanol and co-products at our eight production facilities described below. Our Pacific Ethanol West plants are located on the West Coast near their respective fuel and feed customers, offering significant timing, transportation cost and logistical advantages. Our Pacific Ethanol Central plants are located in the Midwest in the heart of the Corn Belt, benefit from low-cost and abundant feedstock production and allow for access to many additional domestic markets. In addition, our ability to load unit trains from the Pacific Ethanol Central plants allows for greater access to international markets.

	<u>Facility Name</u>	<u>Facility Location</u>	<u>Estimated Annual Capacity (gallons)</u>
<i>Pacific Ethanol West</i>	Magic Valley	Burley, ID	60,000,000
	Columbia	Boardman, OR	40,000,000
	Stockton	Stockton, CA	60,000,000
	Madera	Madera, CA	40,000,000
<i>Pacific Ethanol Central</i>	Aurora West	Aurora, NE	110,000,000
	Aurora East	Aurora, NE	45,000,000
	Pekin Wet	Pekin, IL	100,000,000
	Pekin Dry	Pekin, IL	60,000,000

We produce ethanol co-products at our eight production facilities such as wet distillers grains, or WDG, dry distillers grains with solubles, wet and dry corn gluten feed, condensed distillers solubles, corn gluten meal, corn germ, corn oil, distillers yeast and CO₂.

Marketing Segment

We market ethanol and co-products produced by our eight ethanol production facilities and market ethanol produced by third parties. We have extensive customer relationships throughout the Western and Midwestern United States. Our ethanol customers are integrated oil companies and gasoline marketers who blend ethanol into gasoline. Our customers depend on us to provide a reliable supply of ethanol, and manage the logistics and timing of delivery with very little effort on their part. Our customers collectively require ethanol volumes in excess of the supplies we produce at our eight production facilities. We secure additional ethanol supplies from third party plants in California and other third party suppliers in the Midwest where a majority of ethanol producers are located. We arrange for transportation, storage and delivery of ethanol purchased by our customers through our agreements with third-party service providers in the Western United States as well as in the Midwest from a variety of sources.

We market our distillers grains and other feed co-products to dairies and feedlots, in many cases located near our ethanol plants. These customers use our feed co-products for livestock as a substitute for corn and other sources of starch and protein. We sell our corn oil to poultry and biodiesel customers. We do not market co-products from other ethanol producers.

Current Initiatives and Outlook

We continued to experience a compressed margin environment during the first quarter of 2016. Overall crush margins, which reflect ethanol and co-product sales prices relative to production inputs such as corn and natural gas, remained low during the quarter. This unfavorable margin environment, which affected the ethanol industry as a whole, is primarily due to lower ethanol prices caused by higher industry-wide inventory levels during a period of seasonally low demand. We expect the first quarter of 2016 will be the weakest margin quarter of the year, just as the first quarter of 2015 was the weakest margin quarter of 2015.

We experienced significant margin improvement in the first part of the second quarter due to lower industry-wide production levels and record ethanol demand. We remain confident in the long-term demand for ethanol and its co-products, driven by its underlying economic fundamentals as a high-octane, low-carbon renewable fuel, our ability to execute and create value, and our market position. We are on-track to market more than 800 million gallons of ethanol in 2016 from our expanded production and marketing platform.

The regulatory environment continues to support the long-term demand for renewable fuels. Low-Carbon Fuel Standards in California and Oregon require refiners to reduce the carbon intensity of their fuels in increasing amounts to 10% by 2020 in California and by 2025 in Oregon. We believe this mandate will require a significant amount of low-carbon fuel to displace gasoline in the California and Oregon fuel supplies. Currently, we receive a \$0.10 per gallon premium over Midwest ethanol on each California production gallon sold into the California market. We expect to see a comparable premium for low-carbon ethanol we sell into the Oregon market. In addition, the national Renewable Fuel Standard continues to support the long-term demand for renewable fuels.

We believe our production assets in two distinct markets yield significant benefits, including the ability to spread our commodity and basis price risks across diverse markets and the potential to benefit from regional pricing opportunities resulting from supply imbalances, logistical constraints and feedstock availability. This market diversity enabled us to partially mitigate the effects of the poor margin environment we experienced in the first quarter of 2016. In addition, despite lower distillers grains prices due to reduced demand from China, our diverse portfolio of high-value co-products, including corn oil which adds over \$0.05 per gallon of incremental operating income, provided strong returns and helped mitigate the poor crush margin cycle experienced during the quarter. As margins improve, we believe we are poised to benefit significantly from our larger, more diversified company.

We have undertaken a number of plant improvement initiatives to increase operating efficiencies, enhance yields, improve carbon scores and reduce costs to better position us for sustained profitable operations. In the first quarter, we entered into a technology license and purchase agreement for our Madera facility for an industrial scale membrane system that separates water from ethanol during the plant's dehydration process. We expect this technology to increase operating efficiencies, lower production costs and reduce the carbon intensity of ethanol produced at our Madera facility. Also in the first quarter, we initiated trials of hybrid corn feedstock that contains certain enzymes within the corn kernel to improve our operating performance by reducing corn slurry viscosity and energy consumption. We began producing cellulosic ethanol at our Stockton plant and we are working with our technology provider and the Environmental Protection Agency, or EPA, to qualify this ethanol for special premiums over conventional ethanol. We are also working on cogeneration technology at our Stockton plant, which will convert process waste gas and natural gas into electricity and steam, lowering air emissions and energy costs. We continue to manage our capital spending, focusing on projects that present the highest potential value. Based on market conditions and capital resources, we reduced our capital improvements budget from \$26.0 million to \$15.0 million for 2016. We also may finance capital expenditures through low-cost leases to further reduce our cost of capital, better match our investment profile and the long-term value of our assets, and preserve and improve our liquidity and capital resources.

Net exports of ethanol continue to be a positive factor for the industry. According to the U.S. Energy Information Administration, United States exports of ethanol were 250 million gallons in the first quarter of 2016, representing a 5% year-over-year quarterly increase.

Our goals for 2016 include leveraging our diverse base of production and marketing assets to expand our share of the renewable fuels and ethanol co-product markets; continuing to evaluate and implement new plant improvement initiatives that provide meaningful near-term returns; pursuing opportunities to further strengthen our balance sheet by reducing our cost of capital, efficiently managing cash and improving our overall liquidity position; and further lowering the carbon intensity of our ethanol by modifying existing operations and investing in new technologies such as co-generation, anaerobic digestion and solar power generation, all of which are directed at expanding our share of the renewable fuels market and delivering long-term, profitable growth.

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; warrants and conversion features carried at fair value; impairment of long-lived and intangible assets; valuation of allowance for deferred taxes, derivative instruments, accounting for business combinations 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, 2015.

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 March 31,		Percentage Change
	2016	2015	
Production gallons sold (in millions)	112.9	44.6	153.1%
Third party gallons sold (in millions)	93.7	91.1	2.9%
Total gallons sold (in millions)	206.6	135.7	52.2%
Average sales price per gallon	\$ 1.53	\$ 1.65	(7.3)%
Corn cost per bushel—CBOT equivalent	\$ 3.65	\$ 3.88	(5.9)%
Average basis ⁽¹⁾	0.33	0.93	(64.5)%
Delivered cost of corn	\$ 3.98	\$ 4.81	(17.3)%
Total co-product tons sold (in thousands)	661.4	355.3	86.2%
Co-product revenues as % of delivered cost of corn ⁽²⁾	36.3%	33.8%	7.4%
Average CBOT ethanol price per gallon	\$ 1.39	\$ 1.50	(7.3)%
Average CBOT corn price per bushel	\$ 3.63	\$ 3.85	(5.7)%

(1) Corn basis represents the difference between the immediate cash price of delivered corn and the future price of corn for Chicago delivery.

(2) Co-product revenues as a percentage of delivered cost of corn shows our yield based on sales of co-products, including WDG and corn oil, generated from ethanol we produced.

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 March 31,		Change in	
	2016	2015	Dollars	Percent
Net sales	\$ 342,373	\$ 206,176	\$ 136,197	66.1%
Cost of goods sold	341,304	207,163	134,141	64.8%
Gross profit (loss)	\$ 1,069	\$ (987)	\$ 2,056	NM
<i>Percentage of net sales</i>	<i>0.3%</i>	<i>(0.5)%</i>		

Net Sales

The increase in our net sales for the three months ended March 31, 2016 as compared to the same period in 2015 was due to an increase in our total gallons and co-products sold, partially offset by a decrease in our average sales price per gallon.

We increased both production and third party gallons sold, and our volume of co-products sold, for the three months ended March 31, 2016 as compared to the same period in 2015. The increases in volumes of our production gallons and co-products sold are primarily due to additional volumes from our new Pacific Ethanol Central plants. In addition, we expanded our customer base and our sales to a larger national footprint with the addition of regions we cover with our Midwest plants.

On a consolidated basis, our average sales price per gallon decreased 7.3% to \$1.53 for the three months ended March 31, 2016 compared to our average sales price per gallon of \$1.65 for the same period in 2015. Similarly, the average Chicago Board of Trade, or CBOT, ethanol price per gallon, declined 7.3% to \$1.39 for the three months ended March 31, 2016 compared to an average CBOT sales price per gallon of \$1.50 for the same period in 2015.

Production Segment

Net sales of ethanol from our production segment increased by \$94.1 million, or 128%, to \$167.4 million for the three months ended March 31, 2016 as compared to \$73.3 million for the same period in 2015. Our total volume of production ethanol gallons sold increased by 68.3 million gallons, or 153%, to 112.9 million gallons for the three months ended March 31, 2016 as compared to 44.6 million gallons for the same period in 2015. Our production segment's average sales price per gallon decreased 10.4% to \$1.47 for the three months ended March 31, 2016 compared to our production segment's average sales price per gallon of \$1.64 for the same period in 2015. Of the additional 68.3 million gallons of ethanol sold in the three months ended March 31, 2016, an aggregate of 70.7 million gallons were attributable to production at our Midwestern plants which we acquired on July 1, 2015, slightly offset by 2.4 million fewer gallons produced at our Western plants. At our average sales price per gallon of \$1.47 for the three months ended March 31, 2016, we generated \$100.6 million in additional net sales from our production segment from the 68.3 million additional gallons of produced ethanol sold in the three months ended March 31, 2016 as compared to the same period in 2015. The decline of \$0.17 in our average sales price per gallon for the three months ended March 31, 2016 as compared to the same period in 2015 reduced our net sales of ethanol from our production segment by \$6.5 million.

Net sales of co-products increased \$34.6 million, or 136%, to \$60.1 million for the three months ended March 31, 2016 as compared to \$25.5 million for the same period in 2015. Our total volume of co-products sold increased by 0.3 million tons, or 75%, to 0.7 million tons for three months ended March 31, 2016 from 0.4 million tons for the same period in 2015. At our average sales price per ton of \$87.31 for the three months ended March 31, 2016, we generated \$26.7 million in additional net sales from the 0.3 million additional tons of co-products sold in the three months ended March 31, 2016 as compared to the same period in 2015. In addition, the increase of \$17.85, or 26%, in our average sales price per ton for the three months ended March 31, 2016 as compared to the same period in 2015 increased net sales of co-products by \$7.9 million.

Marketing Segment

Net sales of ethanol from our marketing segment increased by \$5.6 million, or 5%, to \$111.8 million for the three months ended March 31, 2016 as compared to \$106.2 million for the same period in 2015. Our total volume of ethanol gallons sold by our marketing segment increased by 70.9 million gallons, or 52%, to 206.6 million gallons for the three months ended March 31, 2016 as compared to 135.7 million gallons for the same period in 2015. Our additional production gallons sold accounted for 68.3 million gallons of this increase, as noted above, and our additional third-party gallons sold accounted for 2.6 million gallons of this increase.

The increase in production gallons sold by our marketing segment contributed an additional \$1.3 million in net sales generated by our marketing segment, which were eliminated upon consolidation.

Our marketing segment's average sales price per gallon decreased 3.0% to \$1.60 for the three months ended March 31, 2016 compared to our marketing segment's average sales price per gallon of \$1.65 for the same period in 2015. At our average sales price per gallon of \$1.60 for the three months ended March 31, 2016, we generated \$7.3 million in additional net sales from our marketing segment from the 2.6 million gallons in additional third-party ethanol sold in the three months ended March 31, 2016 as compared to the same period in 2015. However, the decline of \$0.05, in our average sales price per gallon for the three months ended March 31, 2016 as compared to the same period in 2015 reduced our net sales from third-party ethanol sold by our marketing segment by \$3.0 million.

Cost of Goods Sold and Gross Profit (Loss)

Our consolidated gross profit increased to \$1.1 million for the three months ended March 31, 2016 as compared to a gross loss of \$1.0 million for the same period in 2015, representing a gross margin of 0.3% for the three months ended March 31, 2016 as compared to negative 0.5% for the same period in 2015. Our consolidated gross profit increased primarily due to slightly higher commodity margins in the three months ended March 31, 2016 compared to the same period in 2015.

Production Segment

Our production segment reduced our consolidated gross profit by \$4.1 million for the three months ended March 31, 2016 as compared to the same period in 2015. Of this amount, \$4.0 million is attributable to the 68.3 million gallon increase in production volumes sold in the three months ended March 31, 2016 as compared to the same period in 2015 and \$0.1 million in lower gross profit is attributed to lower margins resulting primarily from our lower average sales price per gallon in the three months ended March 31, 2016 as compared to the same period in 2015.

Marketing Segment

Our marketing segment increased our consolidated gross profit by \$6.2 million for the three months ended March 31, 2016 as compared to the same period in 2015. Of this amount, \$0.5 million is attributable to additional gross profit from the 4.5 million gallon increase in third-party marketing volumes in the three months ended March 31, 2016 as compared to the same period in 2015 and \$5.7 million in higher gross profit is attributable to our higher margins per gallon for the three months ended March 31, 2016 as compared to the same period in 2015.

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 March 31,		Change in	
	2016	2015	Dollars	Percent
Selling, general and administrative expenses	\$ 8,317	\$ 4,905	\$ 3,412	69.6%
<i>Percentage of net sales</i>	2.4%	2.4%		

Our SG&A increased for the three months ended March 31, 2016 as compared to the same period in 2015. The \$3.4 million period over period increase in SG&A is primarily due to an increase in SG&A associated with our new Pacific Ethanol Central operations, which were not included in the prior period results as the acquisition of Aventine occurred on July 1, 2015. SG&A expenses were greater than our prior guidance of \$7.0 million in part due to higher seasonal professional fees. At current operating levels, including our Pacific Ethanol Central operations, we anticipate SG&A expenses will average approximately \$7.5 million per quarter through the end of 2016.

Interest Expense, net

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

	Three Months Ended March 31,		Change in	
	2016	2015	Dollars	Percent
Interest expense, net	\$ 6,233	\$ 1,015	\$ 5,218	514.1%
<i>Percentage of net sales</i>	1.8%	0.5%		

Interest expense, net increased \$5.2 million to \$6.2 million for the three months ended March 31, 2016 from \$1.0 million for the same period in 2015. The increase in interest expense, net is primarily related to the Pacific Ethanol Central plants' term debt that we assumed, on a consolidated basis, in connection with the acquisition of Aventine.

Benefit for Income Taxes

The following table presents our benefit for income taxes in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended March 31,		Change in	
	2016	2015	Dollars	Percent
Benefit for income taxes	\$ —	\$ 2,700	\$ (2,700)	(100.0%)
<i>Percentage of net sales</i>	<i>—%</i>	<i>1.3%</i>		

For the three months ended March 31, 2015, we recorded a net loss for the period on both a book and tax basis, and recorded a benefit associated with the loss at an estimated tax rate. For the three months ended March 31, 2016, although we incurred a net loss for the period on a book basis, we were not able to carryback these losses to a prior period for an income tax benefit.

Net Loss Attributed to Common Stockholders

The following table presents our net loss attributed to common stockholders in dollars and as a percentage of net sales (in thousands, except percentages):

	Three Months Ended March 31,		Change in	
	2016	2015	Dollars	Percent
Net loss attributed to Common Stockholders	\$ 13,541	\$ 4,692	\$ 8,849	188.6%
<i>Percentage of net sales</i>	<i>4.0%</i>	<i>2.3%</i>		

The increase in net loss attributed to common stockholders was primarily due to our increased SG&A and interest expense costs for the three months ended March 31, 2016, as compared to the same period in 2015.

Liquidity and Capital Resources

During the three months ended March 31, 2016, we funded our operations primarily from cash on hand and proceeds from tax refunds. These funds were also used to make capital expenditures, payments on Kinergy's credit facility, capital lease payments and payments to fully extinguish our term loan balance associated with the Pacific Ethanol West plants.

Our current available capital resources consist of cash on hand and amounts available for borrowing under Kinergy's credit facility. 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 our operations and tax refunds related to prior years.

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.

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):

	March 31, 2016	December 31, 2015	Change
Cash and cash equivalents	\$ 19,207	\$ 52,712	(63.6)%
Current assets	\$ 170,233	\$ 197,942	(14.0)%
Current liabilities	\$ 57,556	\$ 72,909	(21.1)%
Long-term debt, net of current portion	\$ 202,973	\$ 203,861	(0.4)%
Working capital	\$ 112,677	\$ 125,033	(9.9)%
Working capital ratio	2.96	2.71	9.2%

Restricted Net Assets

At March 31, 2016, we had approximately \$145.0 million of net assets at our subsidiaries that were not available to be transferred to the parent company in the form of dividends, loans or advances due to restrictions contained in the credit facilities of these subsidiaries.

Change in Working Capital and Cash Flows

Working capital decreased to \$112.7 million at March 31, 2016 from \$125.0 million at December 31, 2015 as a result of a decrease of \$27.7 million in current assets, partially offset by a decrease of \$15.4 million in current liabilities.

Current assets decreased primarily due to a decrease of \$33.5 million in cash and cash equivalents and a decrease of \$4.5 million in income tax receivable due to tax refunds received, partially offset by increases in inventories of \$8.4 million and accounts receivable of \$2.1 million, both resulting primarily from our new Pacific Ethanol Central operations. The additional inventory and accounts receivable are quickly converted to cash or excess availability under our revolving credit facility, and through the filing of this report, we have approximately \$10.0 million in additional working capital as compared to the end of the first quarter.

Our cash and cash equivalents declined by \$33.5 million at March 31, 2016 as compared to December 31, 2015 due to \$5.2 million of cash used in our operations, \$5.0 million of cash used in our investing activities for our plant improvement initiatives and \$23.4 million of cash used in our financing activities, as discussed below.

Our current liabilities decreased primarily due to a decrease of \$17.0 million in current portion of long-term debt as we extinguished our Pacific Ethanol West plant debt, partially offset by an increase of \$1.5 million in accounts payable and accrued liabilities resulting from our new Pacific Ethanol Central operations.

Cash used in our Operating Activities

Cash used in our operating activities increased by \$12.5 million for the three months ended March 31, 2016 as compared to the same period in 2015. The increase in cash used in our operating activities is primarily due to a higher net loss caused by reduced margins resulting from lower ethanol prices. Additional factors that contributed to the increase in cash used in our operating activities include:

- an increase in accounts receivable of \$9.6 million primarily due to higher sales volumes attributable to our new Pacific Ethanol Central operations; and
- an increase in inventory of \$9.2 million primarily due to higher sales volumes attributable to our new Pacific Ethanol Central operations.

These amounts were partially offset by:

- an increase in depreciation and amortization of \$5.2 million due to additional assets subject to depreciation and amortization from our acquisition of Aventine;
- a decrease in prepaid expenses and other assets of \$8.3 million primarily due to income tax refunds and
- interest expense added to term debt of \$3.8 million.

Cash used in our Investing Activities

Cash used in our investing activities declined by \$3.2 million for the three months ended March 31, 2016 as compared to the same period in 2015. The decline in cash used in our investing activities is primarily due to lower spending on capital projects.

Cash used in our Financing Activities

Cash used in our financing activities increased by \$4.4 million for the three months ended March 31, 2016 as compared to the same period in 2015. The increase in cash used in our financing activities is primarily due to a \$17.0 million principal payment on our term debt associated with the Pacific Ethanol West plants, which was partially offset by a decline of \$12.5 million in payments on Kinergy's line of credit.

Kinergy Operating Line of Credit

Kinergy maintains an operating line of credit for an aggregate amount of up to \$75.0 million. The credit facility expires on December 31, 2020. 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 from 1.75% to 2.75%. The credit facility's monthly unused line fee is 0.25% to 0.375% of the amount by which the maximum credit under the facility exceeds the average daily principal balance during the immediately preceding month. 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 under the terms of the credit facility to \$1.5 million per fiscal quarter. Payments that may be made by Pacific Ag. Products, LLC, or PAP, to Pacific Ethanol as reimbursement for management and other services provided by Pacific Ethanol to PAP are limited under the terms of the credit facility to \$0.5 million per fiscal quarter. PAP, one of our indirect wholly-owned subsidiaries, markets our co-products and also provides raw material procurement services to our subsidiaries. The credit facility also includes the accounts receivable of PAP as additional collateral.

For all monthly periods in which excess availability falls below a specified level, Kinergy and PAP must collectively maintain a fixed-charge coverage ratio (calculated as a twelve-month rolling earnings before interest, taxes, depreciation and amortization (EBITDA) divided by the sum of interest expense, capital expenditures, principal payments of indebtedness, indebtedness from capital leases and taxes paid during such twelve-month rolling period) of at least 2.0 and are prohibited from incurring certain additional indebtedness (other than specific intercompany indebtedness). Kinergy's and PAP's obligations under the credit facility are secured by a first-priority security interest in all of their assets in favor of the lender. Kinergy and PAP believe they are in compliance with this covenant.

The following table summarizes Kinery’s financial covenants and actual results for the periods presented (dollars in thousands):

	Three Months Ended March 31,		Years Ended December 31,	
	2016	2015	2015	2014
Fixed Charge Coverage Ratio Requirement	2.00	2.00	2.00	2.00
Actual	11.68	11.06	10.02	17.66
Excess	9.68	9.06	8.02	15.66

Pacific Ethanol has guaranteed all of Kinery’s obligations under the credit facility. As of March 31, 2016, Kinery had an outstanding balance of \$56.0 million and an available borrowing base under the credit facility of \$63.4 million, representing \$7.4 million of excess availability under the credit facility.

Pacific Ethanol Central Term Debt

On July 1, 2015, upon effectiveness of the Aventine acquisition, Aventine became one of our wholly-owned subsidiaries and, on a consolidated basis, the combined company became obligated with respect to Aventine’s term loan. Aventine’s creditors under Aventine’s term loan have recourse solely against Aventine and its subsidiaries and not against Pacific Ethanol, Inc. or its other direct or indirect subsidiaries.

As of March 31, 2016, the term loan facility for the Pacific Ethanol Central plants had an outstanding balance of approximately \$149.4 million. Interest on the term loan facility accrues and may be paid in cash at a rate of 10.5% per annum or may be paid in-kind at a rate of 15.0% per annum by adding the interest to the outstanding principal balance. If we elect to pay interest in-kind, the interest is capitalized at the end of each quarter. For the three months ended March 31, 2016, we elected to defer interest payments on the term debt in the aggregate amount of \$3.8 million, which was added to the outstanding loan balance. The term loan facility matures on September 24, 2017. The term loan facility is secured through a first-priority lien on substantially all of Aventine’s assets and contains customary financial covenants, and a requirement that Aventine maintain a cash balance of at least \$2.0 million.

We continue to evaluate and pursue opportunities to refinance the term debt for the Pacific Ethanol Central plants.

Contractual Obligations

There have been no material changes in the three months ended March 31, 2016, to the amounts presented in the table under the “Contractual Obligations” section in Part II, Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operation” of our Annual Report on Form 10-K for 2015.

Effects of Inflation

The impact of inflation was not significant to our financial condition or results of operations for the three months ended March 31, 2016 and 2015.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

We are exposed to various market risks, including changes in commodity prices as discussed below. Market risk is the potential loss arising from adverse changes in market rates and prices. In the ordinary course of business, we may enter into various types of transactions involving financial instruments to manage and reduce the impact of changes in commodity prices. We do not expect to have any exposure to foreign currency risk as we conduct all of our transactions in U.S. dollars.

We produce ethanol and ethanol co-products. Our business is sensitive to changes in the prices of each of ethanol and corn. In the ordinary course of business, we may enter into various types of transactions involving financial instruments to manage and reduce the impact of changes in ethanol and corn prices. We do not enter into derivatives or other financial instruments for trading or speculative purposes.

We are subject to market risk with respect to ethanol pricing. Ethanol prices are sensitive to global and domestic ethanol supply, crude-oil supply and demand; crude-oil refining capacity; carbon intensity; government regulation; and consumer demand for alternative fuels. Our ethanol sales are priced using contracts that are either based on a fixed price or an indexed price tied to a specific market, such as CBOT or the Oil Price Information Service. Under these fixed-priced arrangements, we are exposed to risk of a decrease in the market price of ethanol between the time the price is fixed and the time the ethanol is sold.

We satisfy our physical corn needs, the principal raw material used to produce ethanol and ethanol co-products, based on supply-guaranteed contracts with our vendors. Generally, we determine the purchase price of our corn at the time we begin to grind that day's needs. Sometimes, we may also enter into contracts with our vendors to fix a portion of the purchase price of our corn requirements. As such, we are also subject to market risk with respect to the price of corn. The price of corn is subject to wide fluctuations due to unpredictable factors such as weather conditions, farmer planting decisions, governmental policies with respect to agriculture and international trade and global supply and demand. Under the fixed-price arrangements, we assume the risk of a decrease in the market price of corn between the time this price is fixed and the time the corn is utilized.

Ethanol co-products are sensitive to various demand factors such as numbers of livestock on feed, prices for feed alternatives, and supply factors, primarily production of ethanol co-products by ethanol plants and other sources.

As noted above, we may attempt to reduce the market risk associated with fluctuations in the price of ethanol or corn by employing a variety of risk management and hedging strategies. Strategies include the use of derivative financial instruments such as futures and options executed on the CBOT and/or the New York Mercantile Exchange, as well as the daily management of physical corn.

These derivatives are not designated for special hedge accounting treatment, and as such, the changes in the fair values of these contracts are recorded on the balance sheet and recognized immediately in cost of goods sold. We recognized gains of \$0.6 million and losses of \$0.2 million related to settled non-designated hedges as the change in the fair values of these contracts for the three months ended March 31, 2016 and 2015, respectively.

At March 31, 2016, we prepared a sensitivity analysis to estimate our exposure to ethanol and corn. Market risk related to these factors was estimated as the potential change in pre-tax income resulting from a hypothetical 10% adverse change in the prices of our expected ethanol and corn volumes. The results of this analysis as of March 31, 2016, which may differ materially from actual results, are as follows (in millions):

Commodity	Three Months Ended March 31, 2016 Volume	Unit of Measure	Approximate Adverse Change to Pre-Tax Income
Ethanol	206.6	Gallons	\$ 17.4
Corn	40.3	Bushels	\$ 16.0

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 March 31, 2016 that our disclosure controls and procedures were effective at a reasonable assurance level.

Changes in Internal Control over Financial Reporting

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

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 in any material respect our financial position, results of operations or cash flows.

We have evaluated all outstanding cases, including the following pending case and have recorded an aggregate \$3.3 million as a litigation contingency with respect to these cases for amounts that are probable and estimable.

Western Sugar Cooperative

Pacific Ethanol, Inc., through a subsidiary acquired in its acquisition of Aventine, became involved in a pending lawsuit with Western Sugar Cooperative (“Western Sugar”) that pre-dated the Aventine acquisition.

On February 27, 2015, Western Sugar filed a complaint in the United States District Court for the District of Colorado (Case No. 1:15-cv-00415) naming Aventine Renewable Energy, Inc. (“ARE, Inc.”), one of Aventine’s subsidiaries, as defendant. Western Sugar amended its complaint on April 21, 2015. ARE, Inc. purchased surplus sugar through a United States Department of Agriculture program. Western Sugar was one of the entities that warehoused this sugar for ARE, Inc. The suit alleges that ARE, Inc. breached its contract with Western Sugar by failing to pay certain penalty rates for the storage of its sugar or alternatively failing to pay a premium rate for storage. Western Sugar alleges that the penalty rates apply because ARE, Inc. failed to take timely delivery or otherwise cause timely shipment of the sugar. Western Sugar claims “expectation damages” in the amount of approximately \$8.6 million. ARE, Inc. filed answers to Western Sugar’s complaint and amended complaint generally denying Western Sugar’s allegations and asserting various defenses. The case is currently in its discovery phase.

ITEM 1A. RISK FACTORS.

Before deciding to purchase, hold or sell our common stock, you should carefully consider the risks described below in addition to the other information contained in this Report and in our other filings with the Securities and Exchange Commission, including subsequent reports on Forms 10-Q and 8-K. The risks and uncertainties described below are not the only ones we face. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also affect our business. If any of these known or unknown risks or uncertainties actually occurs with material adverse effects on Pacific Ethanol, our business, financial condition, results of operations and/or liquidity could be seriously harmed. In that event, the market price for our common stock will likely decline, and you may lose all or part of your investment.

Risks Related to our Business

We have incurred significant losses and negative operating cash flow in the past and we may incur losses and negative operating cash flow in the future, which may hamper our operations and impede us from expanding our business.

We have incurred significant losses and negative operating cash flow in the past. For the three months ended March 31, 2016 and 2015, we incurred consolidated net losses of \$13.2 million and \$4.5 million, respectively, and for the three months ended March 31, 2016, we incurred negative operating cash flow of \$5.2 million. For the year ended December 31, 2015, we incurred consolidated net losses of approximately \$18.9 million and incurred negative operating cash flows of \$26.8 million. For 2013 and 2012, we incurred consolidated net losses of \$1.2 million and \$43.4 million, respectively, and in 2012 incurred negative operating cash flow of \$20.8 million. We may incur losses and negative operating cash flow in the future. We expect to rely on cash on hand and cash, if any, generated from our operations and from future financing activities to fund all of the cash requirements of our business. Continued losses and negative operating cash flow may hamper our operations and impede us from expanding our business.

Our results of operations and our ability to operate at a profit is largely dependent on managing the costs of corn and natural gas and the prices of ethanol, distillers grains and other ethanol co-products, all of which are subject to significant volatility and uncertainty.

Our results of operations are highly impacted by commodity prices, including the cost of corn and natural gas that we must purchase, and the prices of ethanol, distillers grains and other ethanol co-products that we sell. Prices and supplies are subject to and determined by market and other forces over which we have no control, such as weather, domestic and global demand, supply shortages, export prices and various governmental policies in the United States and around the world.

As a result of price volatility of corn, natural gas, ethanol, distillers grains and other ethanol co-products, our results of operations may fluctuate substantially. In addition, increases in corn or natural gas prices or decreases in ethanol, distillers grains or other ethanol co-product prices may make it unprofitable to operate. In fact, some of our marketing activities will likely be unprofitable in a market of generally declining ethanol prices due to the nature of our business. For example, to satisfy customer demands, we maintain certain quantities of ethanol inventory for subsequent resale. Moreover, we procure much of our inventory outside the context of a marketing arrangement and therefore must buy ethanol at a price established at the time of purchase and sell ethanol at an index price established later at the time of sale that is generally reflective of movements in the market price of ethanol. As a result, our margins for ethanol sold in these transactions generally decline and may turn negative as the market price of ethanol declines.

No assurance can be given that corn or natural gas can be purchased at, or near, current or any particular prices or that ethanol, distillers grains or other ethanol co-products will sell at, or near, current or any particular prices. Consequently, our results of operations and financial position may be adversely affected by increases in the price of corn or natural gas or decreases in the price of ethanol, distillers grains or other ethanol co-products.

Over the past several years, the spread between ethanol and corn prices has fluctuated significantly. Fluctuations are likely to continue to occur. A sustained narrow spread, whether as a result of sustained high or increased corn prices or sustained low or decreased ethanol prices, would adversely affect our results of operations and financial position. Further, combined revenues from sales of ethanol, distillers grains and other ethanol co-products could decline below the marginal cost of production, which may force us to suspend production of ethanol, distillers grains and ethanol co-products at some or all of our plants.

Increased ethanol production may cause a decline in ethanol prices or prevent ethanol prices from rising, and may have other negative effects, adversely impacting our results of operations, cash flows and financial condition.

We believe that the most significant factor influencing the price of ethanol has been the substantial increase in ethanol production in recent years. According to the Renewable Fuels Association, domestic ethanol production capacity increased from an annualized rate of 1.5 billion gallons per year in January 1999 to a record 14.8 billion gallons in 2015. In addition, if ethanol production margins improve, we anticipate that owners of idle ethanol production facilities, many of which may be idled due to poor production margins, will restart operations, thereby resulting in more abundant ethanol supplies and inventories. Any increase in the demand for ethanol may not be commensurate with increases in the supply of ethanol, thus leading to lower ethanol prices. Also, demand for ethanol could be impaired due to a number of factors, including regulatory developments and reduced United States gasoline consumption. Reduced gasoline consumption has occurred in the past and could occur in the future as a result of increased gasoline or oil prices or other factors such as increased automobile fuel efficiency. Any of these outcomes could have a material adverse effect on our results of operations, cash flows and financial condition.

The market price of ethanol is volatile and subject to large fluctuations, which may cause our profitability or losses to fluctuate significantly.

The market price of ethanol is volatile and subject to large fluctuations. The market price of ethanol is dependent upon many factors, including the supply of ethanol and the price of gasoline, which is in turn dependent upon the price of petroleum which is highly volatile and difficult to forecast. For example, ethanol prices, as reported by the CBOT, ranged from \$1.31 to \$1.69 per gallon during 2015 and \$1.50 to \$3.52 per gallon during 2014. Fluctuations in the market price of ethanol may cause our profitability or losses to fluctuate significantly.

Some of our marketing activities will likely be unprofitable in a market of generally declining ethanol prices due to the nature of our business.

Some of our marketing activities will likely be unprofitable in a market of generally declining ethanol prices due to the nature of our business. For example, to satisfy customer demands, we maintain certain quantities of ethanol inventory for subsequent resale. Moreover, we procure much of our inventory outside the context of a marketing arrangement and therefore must buy ethanol at a price established at the time of purchase and sell ethanol at an index price established later at the time of sale that is generally reflective of movements in the market price of ethanol. As a result, our margins for ethanol sold in these transactions generally decline and may turn negative as the market price of ethanol declines.

Disruptions in ethanol production infrastructure may adversely affect our business, results of operations and financial condition.

Our business depends on the continuing availability of rail, road, port, storage and distribution infrastructure. In particular, due to limited storage capacity at our plants and other considerations related to production efficiencies, our plants depend on just-in-time delivery of corn. The production of ethanol also requires a significant and uninterrupted supply of other raw materials and energy, primarily water, electricity and natural gas. The prices of electricity and natural gas have fluctuated significantly in the past and may fluctuate significantly in the future. Local water, electricity and gas utilities may not be able to reliably supply the water, electricity and natural gas that our plants need or may not be able to supply those resources on acceptable terms. Any disruptions in the ethanol production infrastructure, whether caused by labor difficulties, earthquakes, storms, other natural disasters or human error or malfeasance or other reasons, could prevent timely deliveries of corn or other raw materials and energy and may require us to halt production at one or more plants which could have a material adverse effect on our business, results of operations and financial condition.

We may engage in hedging transactions and other risk mitigation strategies that could harm our results of operations.

In an attempt to partially offset the effects of volatility of ethanol prices and corn and natural gas costs, we may enter into contracts to fix the price of a portion of our ethanol production or purchase a portion of our corn or natural gas requirements on a forward basis. In addition, we may engage in other hedging transactions involving exchange-traded futures contracts for corn, natural gas and unleaded gasoline from time to time. The financial statement impact of these activities is dependent upon, among other things, the prices involved and our ability to sell sufficient products to use all of the corn and natural gas for which forward commitments have been made. Hedging arrangements also expose us to the risk of financial loss in situations where the other party to the hedging contract defaults on its contract or, in the case of exchange-traded contracts, where there is a change in the expected differential between the underlying price in the hedging agreement and the actual prices paid or received by us. As a result, our results of operations and financial condition may be adversely affected by fluctuations in the price of corn, natural gas, ethanol and unleaded gasoline.

Operational difficulties at our plants could negatively impact sales volumes and could cause us to incur substantial losses.

Operations at our plants are subject to labor disruptions, unscheduled downtimes and other operational hazards inherent in the ethanol production industry, including equipment failures, fires, explosions, abnormal pressures, blowouts, pipeline ruptures, transportation accidents and natural disasters. Some of these operational hazards may cause personal injury or loss of life, severe damage to or destruction of property and equipment or environmental damage, and may result in suspension of operations and the imposition of civil or criminal penalties. Our insurance may not be adequate to fully cover the potential operational hazards described above or we may not be able to renew this insurance on commercially reasonable terms or at all.

Moreover, our plants may not operate as planned or expected. All of these facilities are designed to operate at or above a specified production capacity. The operation of these facilities is and will be, however, subject to various uncertainties. As a result, these facilities may not produce ethanol and its co-products at expected levels. In the event any of these facilities do not run at their expected capacity levels, our business, results of operations and financial condition may be materially and adversely affected.

Future demand for ethanol is uncertain and may be affected by changes to federal mandates, public perception, consumer acceptance and overall consumer demand for transportation fuel, any of which could negatively affect demand for ethanol and our results of operations.

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 potentially depleting water resources. Some studies have suggested that corn-based ethanol is less efficient than ethanol produced from other feedstock and that it negatively impacts consumers by causing increased prices for dairy, meat and other food generated from livestock that consume corn. Additionally, ethanol critics contend that corn supplies are redirected from international food markets to domestic fuel markets. If negative views of corn-based ethanol production gain acceptance, support for existing measures promoting use and domestic production of corn-based ethanol could decline, leading to reduction or repeal of federal mandates, which could adversely affect the demand for ethanol. These views could also negatively impact public perception of the ethanol industry and acceptance of ethanol as an alternative fuel.

There are limited markets for ethanol beyond those established by federal mandates. Discretionary blending and E85 blending are important secondary markets. Discretionary blending is often determined by the price of ethanol versus the price of gasoline. In periods when discretionary blending is financially unattractive, the demand for ethanol may be reduced. Also, the demand for ethanol is affected by the overall demand for transportation fuel. Demand for transportation fuel is affected by the number of miles traveled by consumers and the fuel economy of vehicles. Market acceptance of E15 may partially offset the effects of decreases in transportation fuel demand. A reduction in the demand for ethanol and ethanol co-products may depress the value of our products, erode our margins and reduce our ability to generate revenue or to operate profitably. Consumer acceptance of E15 and E85 fuels is needed before ethanol can achieve any significant growth in market share relative to other transportation fuels.

If we fail to integrate successfully the businesses of Pacific Ethanol and Aventine our results of operations will be adversely affected.

The success of the Aventine acquisition will depend, in large part, on our ability to realize the anticipated benefits from combining the businesses of Pacific Ethanol and Aventine. To realize these anticipated benefits, we must successfully integrate the businesses of Pacific Ethanol and Aventine. This integration has been and will continue to be complex and time-consuming.

The failure to integrate successfully and to manage successfully the challenges presented by the integration process may result in our failure to achieve some or all of the anticipated benefits of the acquisition.

Potential difficulties that may be encountered in the integration process include the following:

- complexities associated with managing the larger, more complex, combined business;
- integrating personnel;
- potential unknown liabilities and unforeseen expenses, delays or regulatory conditions associated with the acquisition; and
- performance shortfalls as a result of the diversion of management's attention caused by integrating Pacific Ethanol's and Aventine's operations.

Our future results will suffer if we do not effectively manage our expanded operations.

Our business following the Aventine acquisition is significantly larger than the individual businesses of Pacific Ethanol and Aventine prior to the acquisition. Our future success depends, in part, upon our ability to manage our expanded business, which will pose substantial challenges for our management, including challenges related to the management and monitoring of new operations and associated increased costs and complexity. We cannot assure you that we will be successful or that we will realize the expected operating efficiencies, annual net operating synergies, revenue enhancements and other benefits currently anticipated to result from the acquisition.

Our level of indebtedness may make it more difficult for us to pay or refinance our debts and we may need to divert our cash flow from operations to debt service payments. Our indebtedness could limit our ability to pursue other strategic opportunities and could increase our vulnerability to adverse economic and industry conditions.

Our debt service obligations could have an adverse impact on our earnings and cash flows for as long as the indebtedness is outstanding. Our indebtedness could also have important consequences to holders of our common stock. For example, it could:

- make it more difficult to pay or refinance our debts as they become due during adverse economic and industry conditions because any decrease in revenues could cause us to not have sufficient cash flows from operations to make our scheduled debt payments;
- limit our flexibility to pursue other strategic opportunities or react to changes in our business and the industry in which we operate and, consequently, place us at a competitive disadvantage to our competitors who have less debt; or
- require a substantial portion of our cash flows from operations to be used for debt service payments, thereby reducing the availability of our cash flows to fund working capital, capital expenditures, acquisitions, dividend payments and other general corporate purposes.

Based upon current levels of operations, we expect to generate sufficient cash on a consolidated basis to make all principal and interest payments when such payments become due under our existing credit facilities, indentures and other instruments governing our outstanding indebtedness, but there can be no assurance that we will be able to repay or refinance such borrowings and obligations.

If Kinergy fails to satisfy its financial covenants under its credit facility, it may experience a loss or reduction of that facility, which would have a material adverse effect on our financial condition and results of operations.

We are substantially dependent on Kinergy's credit facility to help finance its operations. Kinergy must satisfy monthly financial covenants under its credit facility, including fixed-charge coverage ratio covenants. Kinergy will be in default under its credit facility if it fails to satisfy any financial covenant. A default may result in the loss or reduction of the credit facility. The loss of Kinergy's credit facility, or a significant reduction in Kinergy's borrowing capacity under the facility, would result in Kinergy's inability to finance a significant portion of its business and would have a material adverse effect on our financial condition and results of operations.

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

The EPA has implemented the national Renewable Fuel Standard, or national RFS, pursuant to the Energy Policy Act of 2005 and the Energy Independence and Security Act of 2007. The national RFS program sets annual quotas for the quantity of renewable fuels (such as ethanol) that must be blended into motor fuels consumed in the United States. The domestic market for ethanol is significantly impacted by federal mandates under the national RFS program for volumes of renewable fuels (such as ethanol) required to be blended with gasoline. Future demand for ethanol will be largely dependent upon incentives to blend ethanol into motor fuels, including the relative price of gasoline versus ethanol, the relative octane value of ethanol, constraints in the ability of vehicles to use higher ethanol blends, the national RFS, and other applicable environmental requirements. Any significant increase in production capacity above the national RFS minimum requirements may have an adverse impact on ethanol prices.

Legislation aimed at reducing or eliminating the renewable fuel use required by the national RFS has been introduced in the United States Congress. On January 21, 2015, the *Leave Ethanol Volumes at Existing Levels (LEVEL) Act* (H.R. 434) was introduced in the House. The bill would amend the national RFS by decreasing the required volume of renewable fuels in 2015-2022 to 7.5 billion gallons per year. On February 4, 2015, the *RFS Elimination Act* (H.R. 703) was introduced in the House of Representatives. The bill would fully repeal the national RFS. Also introduced on February 4, 2015, was the *RFS Reform Act* (H.R. 704), which prohibits corn-based ethanol from meeting the national RFS requirements, caps the amount of ethanol that can be blended into conventional gasoline at 10%, and requires the EPA to set requirements for cellulosic biofuels at actual production levels. On January 6, 2015, a bill (H.R. 21) was introduced in the House of Representatives to, among other things, vacate any waivers issued under the Clean Air Act to allow the sale of mid-level ethanol blends for use in motor vehicles. A mid-level ethanol blend is an ethanol-gasoline blend containing 10-20% of ethanol by volume that is intended to be used in any conventional gasoline-powered motor vehicle or nonroad vehicle or engine. On February 26, 2015, the *Corn Ethanol Mandate Elimination Act of 2015* (S. 577) was introduced in the Senate. The bill would eliminate corn ethanol as qualifying as a renewable fuel under the national RFS. *The American Energy Renaissance Act of 2015* (S. 791 and H.R. 1487), which was introduced in the Senate on March 18, 2015 and the House on March 19, 2015, would phase out the national RFS over a five-year period. The *Renewable Fuel Standard Repeal Act* (S. 1584), which would fully repeal the national RFS, was introduced in the Senate on June 16, 2015. All of these bills were assigned to a congressional committee, which will consider them before possibly sending any of them on to the House of Representatives or the Senate as a whole. Our operations could be adversely impacted if any legislation is enacted that reduces or eliminates the national RFS volume requirements or that reduces or eliminates corn ethanol as qualifying as a renewable fuel under the national RFS.

Under the provisions of the Clean Air Act, as amended by the Energy Independence and Security Act of 2007, the EPA has limited authority to waive or reduce the mandated national RFS requirements, which authority is subject to consultation with the Secretaries of Agriculture and Energy, and based on a determination that there is inadequate domestic renewable fuel supply or implementation of the applicable requirements would severely harm the economy or environment of a state, region or the United States. For 2016, the EPA reduced the national RFS from the statutory level of 15.0 billion gallons to 14.0 billion gallons. We believe that the EPA's decision to propose cuts to the congressionally established volumes is based on the EPA's perception that the nation's refueling infrastructure is currently unable to distribute the statutorily-required volumes to consumers. Our results of operations, cash flows and financial condition could be adversely impacted if the EPA further reduces the national RFS requirements from the statutory levels specified in the national RFS.

The ethanol production and marketing industry is extremely competitive. Many of our significant competitors have greater production and financial resources and one or more of these competitors could use their greater resources to gain market share at our expense. In addition, a number of Kinergy's suppliers may circumvent the marketing services we provide, causing our sales and profitability to decline.

The ethanol production and marketing industry is extremely competitive. Many of our significant competitors in the ethanol production and marketing industry, including Archer Daniels Midland Company and Valero Energy Corporation, have substantially greater production and/or financial resources. As a result, our competitors may be able to compete more aggressively and sustain that competition over a longer period of time. Successful competition will require a continued high level of investment in marketing and customer service and support. Our limited resources relative to many significant competitors may cause us to fail to anticipate or respond adequately to new developments and other competitive pressures. This failure could reduce our competitiveness and cause a decline in market share, sales and profitability. Even if sufficient funds are available, we may not be able to make the modifications and improvements necessary to compete successfully.

We also face increasing competition from international suppliers. Currently, international suppliers produce ethanol primarily from sugar cane and have cost structures that are generally substantially lower than our cost structures. Any increase in domestic or foreign competition could cause us to reduce our prices and take other steps to compete effectively, which could adversely affect our business, financial condition and results of operations.

In addition, some of our suppliers are potential competitors and, especially if the price of ethanol reaches historically high levels, they may seek to capture additional profits by circumventing our marketing services in favor of selling directly to our customers. If one or more of our major suppliers, or numerous smaller suppliers, circumvent our marketing services, our sales and profitability may decline.

Our ability to utilize net operating loss carryforwards and certain other tax attributes may be limited.

Federal and state income tax laws impose restrictions on the utilization of net operating loss, or NOL, and tax credit carryforwards in the event that an “ownership change” occurs for tax purposes, as defined by Section 382 of the Internal Revenue Code, or Code. In general, an ownership change occurs when stockholders owning 5% or more of a “loss corporation” (a corporation entitled to use NOL or other loss carryovers) have increased their ownership of stock in such corporation by more than 50 percentage points during any three-year period. The annual base limitation under Section 382 of the Code is calculated by multiplying the loss corporation’s value at the time of the ownership change by the greater of the long-term tax-exempt rate determined by the Internal Revenue Service in the month of the ownership change or the two preceding months.

As of December 31, 2015, we had \$137.6 million of federal NOLs that are limited in their annual use under Section 382 of the Code. Accordingly, our ability to utilize these NOL carryforwards may be substantially limited. These limitations could in turn result in increased future tax obligations, which could have a material adverse effect on our business, financial condition and results of operations.

The high concentration of our sales within the ethanol production and marketing industry could result in a significant reduction in sales and negatively affect our profitability if demand for ethanol declines.

We expect to be completely focused on the production and marketing of ethanol and its co-products for the foreseeable future. We may be unable to shift our business focus away from the production and marketing of ethanol to other renewable fuels or competing products. Accordingly, an industry shift away from ethanol or the emergence of new competing products may reduce the demand for ethanol. A downturn in the demand for ethanol would likely materially and adversely affect our sales and profitability.

We may be adversely affected by environmental, health and safety laws, regulations and liabilities.

We are subject to various federal, state and local environmental laws and regulations, including those relating to the discharge of materials into the air, water and ground, the generation, storage, handling, use, transportation and disposal of hazardous materials and wastes, and the health and safety of our employees. In addition, some of these laws and regulations require us to operate under permits that are subject to renewal or modification. These laws, regulations and permits can often require expensive pollution control equipment or operational changes to limit actual or potential impacts to the environment. A violation of these laws and regulations or permit conditions can result in substantial fines, natural resource damages, criminal sanctions, permit revocations and/or facility shutdowns. In addition, we have made, and expect to make, significant capital expenditures on an ongoing basis to comply with increasingly stringent environmental laws, regulations and permits.

We may be liable for the investigation and cleanup of environmental contamination at each of our plants and at off-site locations where we arrange for the disposal of hazardous substances or wastes. If these substances or wastes have been or are disposed of or released at sites that undergo investigation and/or remediation by regulatory agencies, we may be responsible under the Comprehensive Environmental Response, Compensation and Liability Act of 1980, or other environmental laws for all or part of the costs of investigation and/or remediation, and for damages to natural resources. We may also be subject to related claims by private parties alleging property damage and personal injury due to exposure to hazardous or other materials at or from those properties. Some of these matters may require us to expend significant amounts for investigation, cleanup or other costs.

In addition, new laws, new interpretations of existing laws, increased governmental enforcement of environmental laws or other developments could require us to make significant additional expenditures. Continued government and public emphasis on environmental issues can be expected to result in increased future investments for environmental controls at our plants. Present and future environmental laws and regulations, and interpretations of those laws and regulations, applicable to our operations, more vigorous enforcement policies and discovery of currently unknown conditions may require substantial expenditures that could have a material adverse effect on our results of operations and financial condition.

The hazards and risks associated with producing and transporting our products (including fires, natural disasters, explosions and abnormal pressures and blowouts) may also result in personal injury claims or damage to property and third parties. As protection against operating hazards, we maintain insurance coverage against some, but not all, potential losses. However, we could sustain losses for uninsurable or uninsured risks, or in amounts in excess of existing insurance coverage. Events that result in significant personal injury or damage to our property or third parties or other losses that are not fully covered by insurance could have a material adverse effect on our results of operations and financial condition.

If we are unable to attract or retain key personnel, our ability to operate effectively may be impaired, which could have a material adverse effect on our business, financial condition and results of operations.

Our ability to operate our business and implement strategies depends, in part, on the efforts of our executive officers and other key personnel. Our future success will depend on, among other factors, our ability to retain our current key personnel and attract and retain qualified future key personnel, particularly executive management. In addition, the success of the Aventine acquisition will depend in part on our ability to retain key personnel. It is possible that these personnel might decide not to remain with us now that the acquisition is completed. If these key personnel terminate their employment, our business activities might be adversely affected and management's attention might be diverted from integrating the businesses of Pacific Ethanol and Aventine to recruiting suitable replacement personnel. We may be unable to locate suitable replacements for any such key personnel or offer employment to potential replacement personnel on reasonable terms. If we are unable to attract or retain key personnel, our ability to operate effectively may be impaired, which could have a material adverse effect on our business, financial condition and results of operations.

We depend on a small number of customers for the majority of our sales. A reduction in business from any of these customers could cause a significant decline in our overall sales and profitability.

The majority of our sales are generated from a small number of customers. During 2015, 2014 and 2013, four customers accounted for an aggregate of approximately \$538 million, \$659 million and \$521 million in net sales, representing 45%, 59% and 58% of our net sales, respectively, for those periods. We expect that we will continue to depend for the foreseeable future upon a small number of customers for a significant portion of our sales. Our agreements with these customers generally do not require them to purchase any specified amount of ethanol or dollar amount of sales or to make any purchases whatsoever. Therefore, in any future period, our sales generated from these customers, individually or in the aggregate, may not equal or exceed historical levels. If sales to any of these customers cease or decline, we may be unable to replace these sales with sales to either existing or new customers in a timely manner, or at all. A cessation or reduction of sales to one or more of these customers could cause a significant decline in our overall sales and profitability.

Our lack of long-term ethanol orders and commitments by our customers could lead to a rapid decline in our sales and profitability.

We cannot rely on long-term ethanol orders or commitments by our customers for protection from the negative financial effects of a decline in the demand for ethanol or a decline in the demand for our marketing services. The limited certainty of ethanol orders can make it difficult for us to forecast our sales and allocate our resources in a manner consistent with our actual sales. Moreover, our expense levels are based in part on our expectations of future sales and, if our expectations regarding future sales are inaccurate, we may be unable to reduce costs in a timely manner to adjust for sales shortfalls. Furthermore, because we depend on a small number of customers for a significant portion of our sales, the magnitude of the ramifications of these risks is greater than if our sales were less concentrated. As a result of our lack of long-term ethanol orders and commitments, we may experience a rapid decline in our sales and profitability.

There are limitations on our ability to receive distributions from our subsidiaries.

We conduct most of our operations through subsidiaries and are dependent upon dividends or other intercompany transfers of funds from our subsidiaries to generate free cash flow. Moreover, some of our subsidiaries are limited in their ability to pay dividends or make distributions to us by the terms of their financing arrangements.

Risks Related to Ownership of our Common Stock

Our stock price is highly volatile, which could result in substantial losses for investors purchasing shares of our common stock and in litigation against us.

The market price of our common stock has fluctuated significantly in the past and may continue to fluctuate significantly in the future. The market price of our common stock may continue to fluctuate in response to one or more of the following factors, many of which are beyond our control:

- fluctuations in the market prices of ethanol and its co-products;
- the cost of key inputs to the production of ethanol, including corn and natural gas;
- the volume and timing of the receipt of orders for ethanol from major customers;
- competitive pricing pressures;
- our ability to timely and cost-effectively produce, sell and deliver ethanol;
- the announcement, introduction and market acceptance of one or more alternatives to ethanol;

- losses resulting from adjustments to the fair values of our outstanding warrants to purchase our common stock;
- changes in market valuations of companies similar to us;
- stock market price and volume fluctuations generally;
- the possibility that the anticipated benefits from our acquisition of Aventine cannot be fully realized in a timely manner or at all, or that integrating the acquired operations will be more difficult, disruptive or costly than anticipated;
- regulatory developments or increased enforcement;
- fluctuations in our quarterly or annual operating results;
- additions or departures of key personnel;
- our inability to obtain any necessary financing;
- our financing activities and future sales of our common stock or other securities; and
- our ability to maintain contracts that are critical to our operations.

Furthermore, we believe that the economic conditions in California and other Western states, as well as the United States as a whole, could have a negative impact on our results of operations. Demand for ethanol could also be adversely affected by a slow-down in the overall demand for oxygenate and gasoline additive products. The levels of our ethanol production and purchases for resale will be based upon forecasted demand. Accordingly, any inaccuracy in forecasting anticipated revenues and expenses could adversely affect our business. The failure to receive anticipated orders or to complete delivery in any quarterly period could adversely affect our results of operations for that period. Quarterly results are not necessarily indicative of future performance for any particular period, and we may not experience revenue growth or profitability on a quarterly or an annual basis.

The price at which you purchase shares of our common stock may not be indicative of the price that will prevail in the trading market. You may be unable to sell your shares of common stock at or above your purchase price, which may result in substantial losses to you and which may include the complete loss of your investment. In the past, securities class action litigation has often been brought against a company following periods of high stock price volatility. We may be the target of similar litigation in the future. Securities litigation could result in substantial costs and divert management's attention and our resources away from our business.

Any of the risks described above could have a material adverse effect on our results of operations or the price of our common stock, or both.

We may incur significant non-cash expenses in future periods due to adjustments to the fair values of our outstanding warrants. These non-cash expenses may materially and adversely affect our reported net income or losses and cause our stock price to decline.

From 2010 through 2013, we issued in various financing transactions warrants to purchase shares of our common stock. The warrants were initially recorded at their fair values, which are adjusted quarterly, generally resulting in non-cash expenses or income if the market price of our common stock increases or decreases, respectively, during the period. For example, due to the substantial increase in the market price of our common stock in the first quarter of 2014 and because the exercise prices of these warrants were, as of March 31, 2014, well below the market price of our common stock, the fair values of the warrants and the related non-cash expenses were significantly higher in the first quarter of 2014 than in prior quarterly periods, which resulted in an unusually large non-cash expense for the quarter. These fair value adjustments will continue in future periods until all of our warrants are exercised or expire. We may incur additional significant non-cash expenses in future periods due to adjustments to the fair values of our outstanding warrants resulting from increases in the market price of our common stock during those periods. These non-cash expenses may materially and adversely affect our reported net income or losses and cause our stock price to decline.

The conversion or exercise of our outstanding derivative securities could substantially dilute your investment, reduce your voting power, and, if the resulting shares of common stock are resold into the market, or if a perception exists that a substantial number of shares may be issued and then resold into the market, the market price of our common stock and the value of your investment could decline significantly.

Our outstanding options to acquire our common stock issued to employees, directors and others, and warrants to purchase our common stock, allow the holders of these derivative securities an opportunity to profit from a rise in the market price of our common stock. We have issued common stock in respect of our derivative securities in the past and may do so in the future. If the prices at which our derivative securities are converted or exercised, are lower than the price at which you made your investment, immediate dilution of the value of your investment will occur. Our issuance of shares of common stock under these circumstances will also reduce your voting power. In addition, sales of a substantial number of shares of common stock resulting from any of these issuances, or even the perception that these sales could occur, could adversely affect the market price of our common stock. As a result, you could experience a significant decline in the value of your investment as a result of both the actual and potential issuance of shares of our common stock.

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

Unregistered Sales of Equity Securities

None.

Dividends

Our current and future debt financing arrangements may limit or prevent cash distributions from our subsidiaries to us, depending upon the achievement of specified financial and other operating conditions and our ability to properly service our debt, thereby limiting or preventing us from paying cash dividends.

For each of the three months ended March 31, 2016 and 2015, we declared and paid in cash an aggregate of \$0.3 million in dividends on our Series B Preferred 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. The holders of our outstanding Series B Preferred Stock are entitled to dividends of 7% per annum, payable quarterly. 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.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES.

Not applicable.

ITEM 4. MINE SAFETY DISCLOSURES.

Not applicable.

ITEM 5. OTHER INFORMATION.

None.

ITEM 6. EXHIBITS.

<u>Exhibit Number</u>	<u>Description</u>
10.1	2016 Stock Incentive Plan (*)
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 (*)
101.SCH	XBRL Taxonomy Extension Schema (*)
101.CAL	XBRL Taxonomy Extension Calculation Linkbase (*)
101.DEF	XBRL Taxonomy Extension Definition Linkbase (*)
101.LAB	XBRL Taxonomy Extension Label Linkbase (*)
101.PRE	XBRL Taxonomy Extension Presentation Linkbase (*)

(*) Filed herewith.

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: May 9, 2016

By: /s/ BRYON T. MCGREGOR

Bryon T. McGregor

Chief Financial Officer

(Principal Financial and Accounting Officer)

EXHIBITS FILED WITH THIS REPORT

Exhibit Number	Description
10.1	2016 Stock Incentive Plan
31.1	Certification 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	Certification 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
101.SCH	XBRL Taxonomy Extension Schema
101.CAL	XBRL Taxonomy Extension Calculation Linkbase
101.DEF	XBRL Taxonomy Extension Definition Linkbase
101.LAB	XBRL Taxonomy Extension Label Linkbase
101.PRE	XBRL Taxonomy Extension Presentation Linkbase

**PACIFIC ETHANOL, INC.
2016 STOCK INCENTIVE PLAN**

**ARTICLE ONE
GENERAL PROVISIONS**

I. Purpose of the Plan.

This 2016 Stock Incentive Plan is intended to promote the interests of Pacific Ethanol, Inc. by providing eligible persons in the Corporation's service with the opportunity to acquire a proprietary or economic interest, or otherwise increase their proprietary or economic interest, in the Corporation as an incentive for them to remain in such service and render superior performance during such service. Capitalized terms not otherwise defined herein shall have the meanings assigned to such terms in the attached Appendix.

II. Structure of the Plan.

A. The Plan is divided into two equity-based incentive programs:

- the Discretionary Grant Program, under which eligible persons may, at the discretion of the Plan Administrator, be granted options to purchase shares of common stock or stock appreciation rights tied to the value of such common stock; and
- the Stock Issuance Program, under which eligible persons may be issued shares of common stock pursuant to restricted stock or restricted stock unit awards or other stock-based awards, made by and at the discretion of the Plan Administrator, that vest upon the completion of a designated service period and/or the attainment of pre-established performance milestones, or under which shares of common stock may be issued through direct purchase or as a bonus for services rendered to the Corporation (or any Parent or Subsidiary).

B. The provisions of Articles One and Four shall apply to all equity programs under the Plan and shall govern the interests of all persons under the Plan.

III. Administration of the Plan.

A. The Compensation Committee shall have sole and exclusive authority to administer the Discretionary Grant and Stock Issuance Programs, provided, however, that the Board may retain, reassume or exercise from time to time the power to administer those programs with respect to all persons. However, any discretionary Awards to members of the Compensation Committee must be authorized and approved by a disinterested majority of the Board.

B. The Plan Administrator shall, within the scope of its administrative functions under the Plan, have full power and authority (subject to the provisions of the Plan) to establish such rules and regulations as it may deem appropriate for proper administration of the Discretionary Grant and Stock Issuance Programs and to make such determinations under, and issue such interpretations of, the provisions of those programs and any outstanding Awards thereunder as it may deem necessary or advisable. Decisions of the Plan Administrator within the scope of its administrative functions under the Plan shall be final and binding on all parties who have an interest in the Discretionary Grant and Stock Issuance Programs under its jurisdiction or any Award thereunder.

C. Service on the Compensation Committee shall constitute service as a Board member, and members of each such committee shall accordingly be entitled to full indemnification and reimbursement as Board members for their service on such committee. No member of the Compensation Committee shall be liable for any act or omission made in good faith with respect to the Plan or any Award under the Plan.

IV. Eligibility.

A. The persons eligible to participate in the Discretionary Grant and Stock Issuance Programs are as follows:

- (i) Employees;
- (ii) non-employee members of the Board or the board of directors of any Parent or Subsidiary; and
- (iii) Consultants.

B. The Plan Administrator shall, within the scope of its administrative jurisdiction under the Plan, have full authority to determine (i) with respect to Awards made under the Discretionary Grant Program, which eligible persons are to receive such Awards, the time or times when those Awards are to be made, the number of shares to be covered by each such Award, the status of any awarded option as either an Incentive Option or a Non-Statutory Option, the exercise price per share in effect for each Award (subject to the limitations set forth in Article Two), the time or times when each Award is to vest and become exercisable and the maximum term for which the Award is to remain outstanding, and (ii) with respect to Awards under the Stock Issuance Program, which eligible persons are to receive such Awards, the time or times when the Awards are to be made, the number of shares subject to each such Award, the vesting schedule (if any) applicable to the shares subject to such Award, and the cash consideration (if any) payable for such shares.

C. The Plan Administrator shall have the absolute discretion to grant options or stock appreciation rights in accordance with the Discretionary Grant Program and to effect stock issuances or other stock-based awards in accordance with the Stock Issuance Program.

V. Stock Subject to the Plan.

A. The stock issuable under the Plan shall be shares of authorized but unissued or reacquired common stock, including shares repurchased by the Corporation on the open market. Subject to any additional shares authorized by the vote of the Board and approved by the stockholders, the number of shares of common stock reserved for issuance over the term of the Plan shall not exceed 1,150,000 shares. Any or all of the shares of common stock reserved for issuance under the Plan shall be authorized for issuance pursuant to Incentive Options or other Awards.

B. No one person participating in the Plan may be granted Awards of common stock having a Fair Market Value on the applicable grant date(s) of more than One Million Dollars (\$1,000,000) in the aggregate per calendar year.

C. Shares of common stock subject to outstanding Awards under the Plan shall in no event become eligible for reissuance under the Plan, whether as a result of expiration or termination of an Award, cancellation or repurchase of unvested shares, tender of shares in connection with a net/cashless exercise program, withholding of shares to cover withholding taxes, or otherwise.

D. If any change is made to the common stock by reason of any stock split, stock dividend, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding common stock as a class without the Corporation's receipt of consideration, appropriate adjustments shall be made by the Plan Administrator to (i) the maximum number and/or class of securities issuable under the Plan, (ii) the maximum number and/or class of securities for which any one person may be granted Awards under the Plan per calendar year, (iii) the number and/or class of securities and the exercise or base price per share (or any other cash consideration payable per share) in effect under each outstanding Award under the Discretionary Grant Program, and (iv) the number and/or class of securities subject to each outstanding Award under the Stock Issuance Program and the cash consideration (if any) payable per share thereunder. To the extent such adjustments are to be made to outstanding Awards, those adjustments shall be effected in a manner that shall preclude the enlargement or dilution of rights and benefits under those Awards. The adjustments determined by the Plan Administrator shall be final, binding and conclusive.

VI. Clawback Policy.

The Plan Administrator shall, notwithstanding anything to the contrary contained in any Award document or in any employment or other agreement, have full power and authority to modify or terminate any vested or unvested Award or require repayment to the Corporation of the net proceeds received by a participant arising from any Award, to apply the Corporation's Policy for Recoupment of Incentive Compensation dated March 25, 2011, as such policy may be amended by the Corporation from time to time, or any successor "clawback" or similar policy adopted by the Corporation, including any such policy or policy changes mandated by or implemented pursuant to the Dodd-Frank Wall Street Reform and Consumer Protection Act or the applicable listing requirements or rules and regulations of The NASDAQ Capital Market, if applicable, and any other stock exchange or other market on which common stock is then quoted or listed for trading.

ARTICLE TWO **DISCRETIONARY GRANT PROGRAM**

I. Option Terms.

Each option shall be evidenced by one or more documents in the form approved by the Plan Administrator; provided, however, that each such document shall comply with the terms specified below. Each document evidencing an Incentive Option shall, in addition, be subject to the provisions of the Plan applicable to such options.

A. Exercise Price.

1. The exercise price per share shall be fixed by the Plan Administrator but shall not be less than 85% of the Fair Market Value per share of common stock on the option grant date.

2. The exercise price shall become immediately due upon exercise of the option and shall be payable in one or more of the following forms that the Plan Administrator may deem appropriate in each individual instance:

(i) cash or check made payable to the Corporation;

(ii) shares of common stock valued at Fair Market Value on the Exercise Date and held for the period (if any) necessary to avoid any additional charges to the Corporation's earnings for financial reporting purposes; or

(iii) to the extent the option is exercised for vested shares, through a special sale and remittance procedure pursuant to which the Optionee shall concurrently provide irrevocable instructions to (a) a brokerage firm to effect the immediate sale of the purchased shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the aggregate exercise price payable for the purchased shares plus all applicable federal, state and local income and employment taxes required to be withheld by the Corporation by reason of such exercise and (b) the Corporation to deliver the certificates for the purchased shares directly to such brokerage firm to complete the sale.

Except to the extent such sale and remittance procedure is utilized, payment of the exercise price for the purchased shares must be made on the Exercise Date.

B. Exercise and Term of Options. Each option shall be exercisable at such time or times, during such period and for such number of shares as shall be determined by the Plan Administrator and set forth in the documents evidencing the option. However, no option shall have a term in excess of ten years measured from the option grant date.

C. Effect of Termination of Service.

1. The following provisions shall govern the exercise of any options held by the Optionee at the time of cessation of Service or death:

(i) Any option outstanding at the time of the Optionee's cessation of Service for any reason shall remain exercisable for such period of time thereafter as shall be determined by the Plan Administrator and set forth in the documents evidencing the option or as otherwise specifically authorized by the Plan Administrator in its sole discretion pursuant to an express written agreement with Optionee, but no such option shall be exercisable after the expiration of the option term.

(ii) Any option held by the Optionee at the time of death and exercisable in whole or in part at that time may be subsequently exercised by the personal representative of the Optionee's estate or by the person or persons to whom the option is transferred pursuant to the Optionee's will or the laws of inheritance or by the Optionee's designated beneficiary or beneficiaries of that option.

(iii) During the applicable post-Service exercise period, the option may not be exercised in the aggregate for more than the number of vested shares for which that option is at the time exercisable. No additional shares shall vest under the option following the Optionee's cessation of Service, except to the extent (if any) specifically authorized by the Plan Administrator in its sole discretion pursuant to an express written agreement with Optionee. Upon the expiration of the applicable exercise period or (if earlier) upon the expiration of the option term, the option shall terminate and cease to be outstanding for any shares for which the option has not been exercised.

2. The Plan Administrator shall have complete discretion, exercisable either at the time an option is granted or at any time while the option remains outstanding, to:

(i) extend the period of time for which the option is to remain exercisable following the Optionee's cessation of Service from the limited exercise period otherwise in effect for that option to such greater period of time as the Plan Administrator shall deem appropriate, but in no event beyond the expiration of the option term, and/or

(ii) permit the option to be exercised, during the applicable post-Service exercise period, not only with respect to the number of vested shares of common stock for which such option is exercisable at the time of the Optionee's cessation of Service but also with respect to one or more additional installments in which the Optionee would have vested had the Optionee continued in Service.

D. **Stockholder Rights.** The holder of an option shall have no stockholder rights with respect to the shares subject to the option until such person shall have exercised the option, paid the exercise price and become a holder of record of the purchased shares.

E. **Repurchase Rights.** The Plan Administrator shall have the discretion to grant options that are exercisable for unvested shares of common stock. Should the Optionee cease Service while holding such unvested shares, the Corporation shall have the right to repurchase, at the exercise price paid per share, any or all of those unvested shares. The terms upon which such repurchase right shall be exercisable (including the period and procedure for exercise and the appropriate vesting schedule for the purchased shares) shall be established by the Plan Administrator and set forth in the document evidencing such repurchase right.

F. **Transferability of Options.** The transferability of options granted under the Plan shall be governed by the following provisions:

(i) **Incentive Options.** During the lifetime of the Optionee, Incentive Options shall be exercisable only by the Optionee and shall not be assignable or transferable other than by will or the laws of inheritance following the Optionee's death.

(ii) **Non-Statutory Options.** Non-Statutory Options shall be subject to the same limitation on transfer as Incentive Options, except that the Plan Administrator may structure one or more Non-Statutory Options so that the option may be assigned in whole or in part during the Optionee's lifetime to one or more Family Members of the Optionee or to a trust established exclusively for the Optionee and/or one or more such Family Members, to the extent such assignment is in connection with the Optionee's estate plan or pursuant to a domestic relations order. The assigned portion may only be exercised by the person or persons who acquire a proprietary interest in the option pursuant to the assignment. The terms applicable to the assigned portion shall be the same as those in effect for the option immediately prior to such assignment and shall be set forth in such documents issued to the assignee as the Plan Administrator may deem appropriate.

(iii) **Beneficiary Designations.** Notwithstanding the foregoing, the Optionee may designate one or more persons as the beneficiary or beneficiaries of his or her outstanding options under this Article Two (whether Incentive Options or Non-Statutory Options), and those options shall, in accordance with such designation, automatically be transferred to such beneficiary or beneficiaries upon the Optionee's death while holding those options. Such beneficiary or beneficiaries shall take the transferred options subject to all the terms and conditions of the applicable agreement evidencing each such transferred option, including (without limitation) the limited time period during which the option may be exercised following the Optionee's death.

II. Incentive Options.

The terms specified below, together with any additions, deletions or changes thereto imposed from time to time pursuant to the provisions of the Code governing Incentive Options, shall be applicable to all Incentive Options. Except as modified by the provisions of this Section II, all the provisions of Articles One, Two and Four shall be applicable to Incentive Options. Options that are specifically designated as Non-Statutory Options when issued under the Plan shall not be subject to the terms of this Section II.

A. **Eligibility.** Incentive Options may only be granted to Employees.

B. **Exercise Price.** The exercise price per share shall not be less than 100% of the Fair Market Value per share of common stock on the option grant date.

C. **Dollar Limitation.** The aggregate Fair Market Value of the shares of common stock (determined as of the respective date or dates of grant) for which one or more options granted to any Employee under the Plan (or any other option plan of the Corporation or any Parent or Subsidiary) may for the first time become exercisable as Incentive Options during any one calendar year shall not exceed the sum of One Hundred Thousand Dollars (\$100,000). To the extent the Employee holds two or more such options which become exercisable for the first time in the same calendar year, then for purposes of the foregoing limitation on the exercisability of those options as Incentive Options, such options shall be deemed to become first exercisable in that calendar year on the basis of the chronological order in which they were granted, except to the extent otherwise provided under applicable law or regulation.

D. **10% Stockholder.** If any Employee to whom an Incentive Option is granted is a 10% Stockholder, then the exercise price per share shall not be less than 110% of the Fair Market Value per share of common stock on the option grant date, and the option term shall not exceed five years measured from the option grant date.

III. **Stock Appreciation Rights.**

A. **Authority.** The Plan Administrator shall have full power and authority, exercisable in its sole discretion, to grant stock appreciation rights in accordance with this Section III to selected Optionees or other individuals eligible to receive option grants under the Discretionary Grant Program.

B. **Types.** Three types of stock appreciation rights shall be authorized for issuance under this Section III: (i) tandem stock appreciation rights ("Tandem Rights"), (ii) standalone stock appreciation rights ("Standalone Rights") and (iii) limited stock appreciation rights ("Limited Rights").

C. **Tandem Rights.** The following terms and conditions shall govern the grant and exercise of Tandem Rights.

1. One or more Optionees may be granted a Tandem Right, exercisable upon such terms and conditions as the Plan Administrator may establish, to elect between the exercise of the underlying stock option for shares of common stock or the surrender of that option in exchange for a distribution from the Corporation in an amount equal to the excess of (i) the Fair Market Value (on the option surrender date) of the number of shares in which the Optionee is at the time vested under the surrendered option (or surrendered portion thereof) over (ii) the aggregate exercise price payable for such vested shares.

2. No such option surrender shall be effective unless it is approved by the Plan Administrator, either at the time of the actual option surrender or at any earlier time. If the surrender is so approved, then the distribution to which the Optionee shall accordingly become entitled under this Section III may be made in shares of common stock valued at Fair Market Value on the option surrender date, in cash, or partly in shares and partly in cash, as the Plan Administrator shall in its sole discretion deem appropriate.

3. If the surrender of an option is not approved by the Plan Administrator, then the Optionee shall retain whatever rights the Optionee had under the surrendered option (or surrendered portion thereof) on the option surrender date and may exercise such rights at any time prior to the later of (i) five business days after the receipt of the rejection notice or (ii) the last day on which the option is otherwise exercisable in accordance with the terms of the instrument evidencing such option, but in no event may such rights be exercised more than ten years after the date of the option grant.

D. **Standalone Rights.** The following terms and conditions shall govern the grant and exercise of Standalone Rights under this Article Two:

1. One or more individuals eligible to participate in the Discretionary Grant Program may be granted a Standalone Right not tied to any underlying option under this Discretionary Grant Program. The Standalone Right shall relate to a specified number of shares of common stock and shall be exercisable upon such terms and conditions as the Plan Administrator may establish. In no event, however, may the Standalone Right have a maximum term in excess of ten years measured from the grant date. Upon exercise of the Standalone Right, the holder shall be entitled to receive a distribution from the Corporation in an amount equal to the excess of (i) the aggregate Fair Market Value (on the exercise date) of the shares of common stock underlying the exercised right over (ii) the aggregate base price in effect for those shares.

2. The number of shares of common stock underlying each Standalone Right and the base price in effect for those shares shall be determined by the Plan Administrator in its sole discretion at the time the Standalone Right is granted. In no event, however, may the base price per share be less than the Fair Market Value per underlying share of common stock on the grant date.

3. Standalone Rights shall be subject to the same transferability restrictions applicable to Non-Statutory Options and may not be transferred during the holder's lifetime, except to one or more Family Members of the holder or to a trust established exclusively for the holder and/or such Family Members, to the extent such assignment is in connection with the holder's estate plan or pursuant to a domestic relations order covering the Standalone Right as marital property. In addition, one or more beneficiaries may be designated for an outstanding Standalone Right in accordance with substantially the same terms and provisions as set forth in Section I.F of this Article Two.

4. The distribution with respect to an exercised Standalone Right may be made in shares of common stock valued at Fair Market Value on the exercise date, in cash, or partly in shares and partly in cash, as the Plan Administrator shall in its sole discretion deem appropriate.

5. The holder of a Standalone Right shall have no stockholder rights with respect to the shares subject to the Standalone Right unless and until such person shall have exercised the Standalone Right and become a holder of record of shares of common stock issued upon the exercise of such Standalone Right.

E. **Limited Rights.** The following terms and conditions shall govern the grant and exercise of Limited Rights under this Article Two:

1. One or more Section 16 Insiders may, in the Plan Administrator's sole discretion, be granted Limited Rights with respect to their outstanding options under this Article Two.

2. Upon the occurrence of a Hostile Take-Over, the Section 16 Insider shall have the unconditional right (exercisable for a 30-day period following such Hostile Take-Over) to surrender each option with such a Limited Right to the Corporation. The Section 16 Insider shall in return be entitled to a cash distribution from the Corporation in an amount equal to the excess of (i) the Take-Over Price of the number of shares in which the Optionee is at the time vested under the surrendered option (or surrendered portion thereof) over (ii) the aggregate exercise price payable for those vested shares. Such cash distribution shall be made within five days following the option surrender date.

3. The Plan Administrator shall pre-approve, at the time such Limited Right is granted, the subsequent exercise of that right in accordance with the terms of the grant and the provisions of this Section III. No additional approval of the Plan Administrator or the Board shall be required at the time of the actual option surrender and cash distribution. Any unsurrendered portion of the option shall continue to remain outstanding and become exercisable in accordance with the terms of the instrument evidencing such grant.

F. **Post-Service Exercise.** The provisions governing the exercise of Tandem, Standalone and Limited Stock Appreciation Rights following the cessation of the recipient's Service or the recipient's death shall be substantially the same as those set forth in Section I.C of this Article Two for the options granted under the Discretionary Grant Program.

IV. Change in Control/ Hostile Take-Over.

A. No Award outstanding under the Discretionary Grant Program at the time of a Change in Control shall vest and become exercisable on an accelerated basis if and to the extent that: (i) such Award is, in connection with the Change in Control, assumed by the successor corporation (or parent thereof) or otherwise continued in full force and effect pursuant to the terms of the Change in Control transaction, (ii) such Award is replaced with a cash retention program of the successor corporation that preserves the spread existing at the time of the Change in Control on the shares of common stock as to which the Award is not otherwise at that time vested and exercisable and provides for subsequent payout of that spread in accordance with the same exercise/vesting schedule applicable to those shares, or (iii) the acceleration of such Award is subject to other limitations imposed by the Plan Administrator. However, if none of the foregoing conditions are satisfied, each Award outstanding under the Discretionary Grant Program at the time of the Change in Control but not otherwise vested and exercisable as to all the shares at the time subject to that Award shall automatically accelerate so that each such Award shall, immediately prior to the effective date of the Change in Control, vest and become exercisable as to all the shares of common stock at the time subject to that Award and may be exercised as to any or all of those shares as fully vested shares of common stock.

B. All outstanding repurchase rights under the Discretionary Grant Program shall also terminate automatically, and the shares of common stock subject to those terminated rights shall immediately vest in full, in the event of any Change in Control, except to the extent: (i) those repurchase rights are assigned to the successor corporation (or parent thereof) or otherwise continue in full force and effect pursuant to the terms of the Change in Control transaction or (ii) such accelerated vesting is precluded by other limitations imposed by the Plan Administrator.

C. Immediately following the consummation of the Change in Control, all outstanding Awards under the Discretionary Grant Program shall terminate and cease to be outstanding, except to the extent assumed by the successor corporation (or parent thereof) or otherwise expressly continued in full force and effect pursuant to the terms of the Change in Control transaction.

D. Each option that is assumed in connection with a Change in Control or otherwise continued in effect shall be appropriately adjusted, immediately after such Change in Control, to apply to the number and class of securities that would have been issuable to the Optionee in consummation of such Change in Control had the option been exercised immediately prior to such Change in Control. In the event outstanding Standalone Rights are to be assumed in connection with a Change in Control transaction or otherwise continued in effect, the shares of common stock underlying each such Standalone Right shall be adjusted immediately after such Change in Control to apply to the number and class of securities into which those shares of common stock would have been converted in consummation of such Change in Control had those shares actually been outstanding at that time. Appropriate adjustments to reflect such Change in Control shall also be made to (i) the exercise price payable per share under each outstanding option, provided the aggregate exercise price payable for such securities shall remain the same, (ii) the base price per share in effect under each outstanding Standalone Right, provided the aggregate base price shall remain the same, (iii) the maximum number and/or class of securities available for issuance over the remaining term of the Plan, and (iv) the maximum number and/or class of securities for which any one person may be granted Awards under the Plan per calendar year. To the extent the actual holders of the Corporation's outstanding common stock receive cash consideration for their common stock in consummation of the Change in Control, the successor corporation may, in connection with the assumption or continuation of the outstanding Awards under the Discretionary Grant Program, substitute, for the securities underlying those assumed Awards, one or more shares of its own common stock with a fair market value equivalent to the cash consideration paid per share of common stock in such Change in Control transaction.

E. The Plan Administrator shall have full power and authority to structure one or more outstanding Awards under the Discretionary Grant Program so that those Awards shall immediately vest and become exercisable as to all of the shares at the time subject to those Awards in the event the Optionee's Service is subsequently terminated by reason of an Involuntary Termination within a designated period (not to exceed 18 months) following the effective date of any Change in Control or a Hostile Take-Over in which those Awards do not otherwise vest on an accelerated basis. Any Awards so accelerated shall remain exercisable as to fully vested shares until the expiration or sooner termination of their term. In addition, the Plan Administrator may structure one or more of the Corporation's repurchase rights under the Discretionary Grant Program so that those rights shall immediately terminate with respect to any shares held by the Optionee at the time of his or her Involuntary Termination, and the shares subject to those terminated repurchase rights shall accordingly vest in full at that time.

F. The portion of any Incentive Option accelerated in connection with a Change in Control shall remain exercisable as an Incentive Option only to the extent the applicable One Hundred Thousand Dollar (\$100,000) limitation is not exceeded. To the extent such dollar limitation is exceeded, the accelerated portion of such option shall be exercisable as a Non-Statutory Option under the federal tax laws.

G. Awards outstanding under the Discretionary Grant Program shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

ARTICLE THREE **STOCK ISSUANCE PROGRAM**

I. Stock Issuance Terms.

A. **Issuances.** Shares of common stock may be issued under the Stock Issuance Program through direct and immediate issuances without any intervening option grants. Each such stock issuance shall be evidenced by a Stock Issuance Agreement that complies with the terms specified below. Shares of common stock may also be issued under the Stock Issuance Program pursuant to restricted stock awards or restricted stock units, awarded by and at the discretion of the Plan Administrator, that entitle the recipients to receive the shares underlying those awards or units upon the attainment of designated performance goals and/or the satisfaction of specified Service requirements or upon the expiration of a designated time period following the vesting of those awards or units.

B. Issue Price.

1. The price per share at which shares of common stock may be issued under the Stock Issuance Program shall be fixed by the Plan Administrator, but shall not be less than 100% of the Fair Market Value per share of common stock on the issuance date.

2. Shares of common stock may be issued under the Stock Issuance Program for any of the following items of consideration that the Plan Administrator may deem appropriate in each individual instance:

(i) cash or check made payable to the Corporation;

(ii) past services rendered to the Corporation (or any Parent or Subsidiary); or

(iii) any other valid form of consideration permissible under the Delaware Corporations Code at the time such shares are issued.

C. Vesting Provisions.

1. Shares of common stock issued under the Stock Issuance Program may, in the discretion of the Plan Administrator, be fully and immediately vested upon issuance or may vest in one or more installments over the Participant's period of Service and/or upon attainment of specified performance objectives. The elements of the vesting schedule applicable to any unvested shares of common stock issued under the Stock Issuance Program shall be determined by the Plan Administrator and incorporated into the Stock Issuance Agreement. Shares of common stock may also be issued under the Stock Issuance Program pursuant to restricted stock awards or restricted stock units that entitle the recipients to receive the shares underlying those awards and/or units upon the attainment of designated performance goals or the satisfaction of specified Service requirements or upon the expiration of a designated time period following the vesting of those awards or units, including (without limitation) a deferred distribution date following the termination of the Participant's Service.

2. The Plan Administrator shall also have the discretionary authority, consistent with Code Section 162(m), to structure one or more Awards under the Stock Issuance Program so that the shares of common stock subject to those Awards shall vest (or vest and become issuable) upon the achievement of certain pre-established corporate performance goals based on one or more of the following criteria: (i) return on total stockholders' equity; (ii) net income per share of common stock; (iii) net income or operating income; (iv) earnings before interest, taxes, depreciation, amortization and stock-compensation costs, or operating income before depreciation and amortization; (v) sales or revenue targets; (vi) return on assets, capital or investment; (vii) cash flow; (viii) market share; (ix) cost reduction goals; (x) budget comparisons; (xi) implementation or completion of projects or processes strategic or critical to the Corporation's business operations; (xii) measures of customer satisfaction; (xiii) any combination of, or a specified increase in, any of the foregoing; and (xiv) the formation of joint ventures, research and development collaborations, marketing or customer service collaborations, or the completion of other corporate transactions intended to enhance the Corporation's revenue or profitability or expand its customer base; provided, however, that for purposes of items (ii), (iii) and (vii) above, the Plan Administrator may, at the time the Awards are made, specify certain adjustments to such items as reported in accordance with generally accepted accounting principles in the U.S. ("GAAP"), which will exclude from the calculation of those performance goals one or more of the following: certain charges related to acquisitions, stock-based compensation, employer payroll tax expense on certain stock option exercises, settlement costs, restructuring costs, gains or losses on strategic investments, non-operating gains or losses, certain other non-cash charges, valuation allowance on deferred tax assets, and the related income tax effects, purchases of property and equipment, and any extraordinary non-recurring items as described in Accounting Principles Board Opinion No. 30 or its successor, provided that such adjustments are in conformity with those reported by the Corporation on a non-GAAP basis. In addition, such performance goals may be based upon the attainment of specified levels of the Corporation's performance under one or more of the measures described above relative to the performance of other entities and may also be based on the performance of any of the Corporation's business groups or divisions thereof or any Parent or Subsidiary. Performance goals may include a minimum threshold level of performance below which no award will be earned, levels of performance at which specified portions of an award will be earned, and a maximum level of performance at which an award will be fully earned. The Plan Administrator may provide that, if the actual level of attainment for any performance objective is between two specified levels, the amount of the award attributable to that performance objective shall be interpolated on a straight-line basis.

3. Any new, substituted or additional securities or other property (including money paid other than as a regular cash dividend) that the Participant may have the right to receive with respect to the Participant's unvested shares of common stock by reason of any stock dividend, stock split, recapitalization, combination of shares, exchange of shares or other change affecting the outstanding common stock as a class without the Corporation's receipt of consideration shall be issued subject to (i) the same vesting requirements applicable to the Participant's unvested shares of common stock and (ii) such escrow arrangements as the Plan Administrator shall deem appropriate.

4. The Participant shall have full stockholder rights with respect to any shares of common stock issued to the Participant under the Stock Issuance Program, whether or not the Participant's interest in those shares is vested. Accordingly, the Participant shall have the right to vote such shares and to receive any regular cash dividends paid on such shares. The Participant shall not have any stockholder rights with respect to the shares of common stock subject to a restricted stock unit award until that award vests and the shares of common stock are actually issued thereunder. However, dividend-equivalent units may be paid or credited, either in cash or in actual or phantom shares of common stock, on outstanding restricted stock unit or restricted stock awards, subject to such terms and conditions as the Plan Administrator may deem appropriate.

5. Should the Participant cease to remain in Service while holding one or more unvested shares of common stock issued under the Stock Issuance Program or should the performance objectives not be attained with respect to one or more such unvested shares of common stock, then except as set forth in Section I.C.6 of this Article Three, those shares shall be immediately surrendered to the Corporation for cancellation, and the Participant shall have no further stockholder rights with respect to those shares. To the extent the surrendered shares were previously issued to the Participant for consideration paid in cash, cash equivalent or otherwise, the Corporation shall repay to the Participant the same amount and form of consideration as the Participant paid for the surrendered shares.

6. The Plan Administrator may in its discretion waive the surrender and cancellation of one or more unvested shares of common stock that would otherwise occur upon the cessation of the Participant's Service or the non-attainment of the performance objectives applicable to those shares. Any such waiver shall result in the immediate vesting of the Participant's interest in the shares of common stock as to which the waiver applies. Such waiver may be effected at any time, whether before or after the Participant's cessation of Service or the attainment or non-attainment of the applicable performance objectives. However, no vesting requirements tied to the attainment of performance objectives may be waived with respect to shares that were intended at the time of issuance to qualify as performance-based compensation under Code Section 162(m), except in the event of the Participant's Involuntary Termination or as otherwise provided in Section II.E of this Article Three.

7. Outstanding restricted stock awards or restricted stock units under the Stock Issuance Program shall automatically terminate, and no shares of common stock shall actually be issued in satisfaction of those awards or units, if the performance goals or Service requirements established for such awards or units are not attained or satisfied. The Plan Administrator, however, shall have the discretionary authority to issue vested shares of common stock under one or more outstanding restricted stock awards or restricted stock units as to which the designated performance goals or Service requirements have not been attained or satisfied. However, no vesting requirements tied to the attainment of performance goals may be waived with respect to awards or units which were at the time of grant intended to qualify as performance-based compensation under Code Section 162(m), except in the event of the Participant's Involuntary Termination or as otherwise provided in Section II.E of this Article Three.

II. Change in Control/ Hostile Take-Over.

A. All of the Corporation's outstanding repurchase rights under the Stock Issuance Program shall terminate automatically, and all the shares of common stock subject to those terminated rights shall immediately vest in full, in the event of any Change in Control, except to the extent (i) those repurchase rights are to be assigned to the successor corporation (or parent thereof) or otherwise continued in full force and effect pursuant to the express terms of the Change in Control transaction or (ii) such accelerated vesting is precluded by other limitations imposed in the Stock Issuance Agreement.

B. Each outstanding Award under the Stock Issuance Program that is assumed in connection with a Change in Control or otherwise continued in effect shall be adjusted immediately after the consummation of that Change in Control to apply to the number and class of securities into which the shares of common stock subject to the Award immediately prior to the Change in Control would have been converted in consummation of such Change in Control had those shares actually been outstanding at that time, and appropriate adjustments shall also be made to the cash consideration (if any) payable per share thereunder, provided the aggregate amount of such consideration shall remain the same. If any such Award is not so assumed or otherwise continued in effect or replaced with a cash retention program which preserves the Fair Market Value of the shares underlying the Award at the time of the Change in Control and provides for the subsequent payout of that value in accordance with the vesting schedule in effect for the Award at the time of such Change in Control, such Award shall vest, and the shares of common stock subject to that Award shall be issued as fully-vested shares, immediately prior to the consummation of the Change in Control.

C. The Plan Administrator shall have full power and authority to structure one or more outstanding Awards under the Stock Issuance Program so that the shares of common stock subject to those Awards shall immediately vest (or vest and become issuable) as to all of the shares at the time subject to those Awards in the event the Participant's Service is subsequently terminated by reason of an Involuntary Termination within a designated period (not to exceed 18 months) following the effective date of any Change in Control or a Hostile Take-Over in which those Awards do not otherwise vest on an accelerated basis. In addition, the Plan Administrator may structure one or more of the Corporation's repurchase rights under the Stock Issuance Program so that those rights shall immediately terminate with respect to any shares held by the Participant at the time of his or her Involuntary Termination, and the shares subject to those terminated repurchase rights shall accordingly vest in full at that time.

D. The Plan Administrator's authority under Paragraph C of this Section II shall also extend to any Award intended to qualify as performance-based compensation under Code Section 162(m), even though the automatic vesting of those Awards pursuant to Paragraph C of this Section II may result in their loss of performance-based status under Code Section 162(m).

E. Awards outstanding under the Stock Issuance Program shall in no way affect the right of the Corporation to adjust, reclassify, reorganize or otherwise change its capital or business structure or to merge, consolidate, dissolve, liquidate or sell or transfer all or any part of its business or assets.

ARTICLE FOUR **MISCELLANEOUS**

I. Tax Withholding.

A. The Corporation's obligation to deliver shares of common stock upon the issuance, exercise or vesting of Awards under the Plan shall be subject to the satisfaction of all applicable federal, state and local income and employment tax withholding requirements.

B. Subject to applicable laws, rules and regulations and policies of the Corporation, the Plan Administrator may, in its discretion, provide any or all Optionees or Participants to whom Awards are made under the Plan with the right to utilize any or all of the following methods to satisfy all or part of the Withholding Taxes to which those holders may become subject in connection with the issuance, exercise or vesting of those Awards.

(i) *Stock Withholding*: The election to have the Corporation withhold, from the shares of common stock otherwise issuable upon the issuance, exercise or vesting of those Awards a portion of those shares with an aggregate Fair Market Value equal to the percentage of the Withholding Taxes (not to exceed 100%) designated by the Optionee or Participant and make a cash payment equal to such Fair Market Value directly to the appropriate taxing authorities on such individual's behalf.

(ii) *Stock Delivery*: The election to deliver to the Corporation, at the time the Award is issued, exercised or vests, one or more shares of common stock previously acquired by such the Optionee or Participant (other than in connection with the issuance, exercise or vesting triggering the Withholding Taxes) with an aggregate Fair Market Value equal to the percentage of the Withholding Taxes (not to exceed 100%) designated by such holder. The shares of common stock so delivered shall not be added to the shares of common stock authorized for issuance under the Plan.

(iii) *Sale and Remittance*: The election to deliver to the Corporation, to the extent the Award is issued or exercised for vested shares, through a special sale and remittance procedure pursuant to which the Optionee or Participant shall concurrently provide irrevocable instructions to a brokerage firm to effect the immediate sale of the purchased or issued shares and remit to the Corporation, out of the sale proceeds available on the settlement date, sufficient funds to cover the Withholding Taxes required to be withheld by the Corporation by reason of such issuance, exercise or vesting.

II. Share Escrow/Legends.

Unvested shares issued under the Plan may, in the Plan Administrator's discretion, be held in escrow by the Corporation until the Participant's interest in such shares vests or may be issued directly to the Participant with restrictive legends on the certificates evidencing those unvested shares.

III. Effective Date and Term of the Plan.

A. The Plan was adopted by the Board on March 25, 2016, subject to stockholder approval within twelve months after that date. Should stockholder approval not be obtained within such period, the Plan will be terminated.

B. The Plan shall become effective on the Plan Effective Date. Awards may be granted under the Discretionary Grant Program and the Stock Issuance Program at any time on or after the Plan Effective Date.

C. The Plan shall terminate upon the earliest to occur of (i) March 25, 2017, if stockholder approval of the Plan has not been obtained on or prior to that date, (ii) March 25, 2026, (iii) the date on which all shares available for issuance under the Plan shall have been issued as fully-vested shares, (iv) the termination of all outstanding Awards in connection with a Change in Control, or (v) such other date as the Board in its sole discretion terminates the Plan. If the Plan terminates on March 25, 2026 or on such other date as the Board terminates the Plan, then all Awards outstanding at that time shall continue to have force and effect in accordance with the provisions of the documents evidencing such Awards.

IV. Amendment, Suspension or Termination of the Plan.

The Board may suspend or terminate the Plan at any time, without notice, and in its sole discretion. The Board shall have complete and exclusive power and authority to amend or modify the Plan in any or all respects. However, no such amendment or modification shall materially impair the rights and obligations with respect to Awards at the time outstanding under the Plan unless the Optionee or the Participant consents to such amendment or modification. In addition, stockholder approval will be required for any amendment to the Plan that (i) materially increases the number of shares of common stock available for issuance under the Plan, (ii) materially expands the class of individuals eligible to receive option grants or other awards under the Plan, (iii) materially increases the benefits accruing to the Optionees and Participants under the Plan or materially reduces the price at which shares of common stock may be issued or purchased under the Plan, (iv) materially extends the term of the Plan, (v) expands the types of awards available for issuance under the Plan or (vi) is required under applicable laws, rules or regulations to be approved by stockholders.

V. Use of Proceeds.

Any cash proceeds received by the Corporation from the sale of shares of common stock under the Plan shall be used for general corporate purposes.

VI. Regulatory Approvals.

A. The implementation of the Plan, the grant of any Award and the issuance of shares of common stock in connection with the issuance, exercise or vesting of any Award made under the Plan shall be subject to the Corporation's procurement of all approvals and permits required by regulatory authorities having jurisdiction over the Plan, the Awards made under the Plan and the shares of common stock issuable pursuant to those Awards.

B. No shares of common stock or other assets shall be issued or delivered under the Plan unless and until there shall have been compliance with all applicable requirements of federal and state securities laws, including the filing and effectiveness of the Form S-8 registration statement for the shares of common stock issuable under the Plan, and all applicable listing requirements of The NASDAQ Capital Market, if applicable, and any other stock exchange or other market on which common stock is then quoted or listed for trading.

VII. No Employment/Service Rights.

Nothing in the Plan shall confer upon the Optionee or the Participant any right to continue in Service for any period of specific duration or interfere with or otherwise restrict in any way the rights of the Corporation (or any Parent or Subsidiary employing or retaining such person) or of the Optionee or the Participant, which rights are hereby expressly reserved by each, to terminate such person's Service at any time for any reason, with or without cause.

VIII. Non-Exclusivity of the Plan.

Nothing contained in the Plan is intended to amend, modify, or rescind any previously approved compensation plans, programs or options entered into by the Corporation. This Plan shall be construed to be in addition to and independent of any and all other arrangements. Neither the adoption of the Plan by the Board nor the submission of the Plan to the stockholders of the Corporation for approval shall be construed as creating any limitations on the power or authority of the Board to adopt, with or without stockholder approval, such additional or other compensation arrangements as the Board may from time to time deem desirable.

IX. Governing Law.

All questions and obligations under the Plan and agreements issued pursuant to the Plan shall be construed and enforced in accordance with the laws of the State of Delaware.

X. Information to Optionees and Participants.

Optionees and Participants under the Plan who do not otherwise have access to financial statements of the Corporation will receive the Corporation's financial statements at least annually.

APPENDIX

The following definitions shall be in effect under the Plan:

A. "Award" means any of the following stock or stock-based awards authorized for issuance or grant under the Plan: stock option, stock appreciation right, direct stock issuance, restricted stock or restricted stock unit award or other stock-based award.

B. "Board" means the Corporation's board of directors.

C. "Change in Control" shall be deemed to have occurred if, in a single transaction or series of related transactions:

(i) any person (as such term is used in Section 13(d) and 14(d) of the 1934 Act, or persons acting as a group, other than a trustee or fiduciary holding securities under an employment benefit program, is or becomes a "beneficial owner" (as defined in Rule 13-3 under the 1934 Act), directly or indirectly of securities of the Corporation representing 51% or more of the combined voting power of the Corporation, or

(ii) there is a merger, consolidation, or other business combination transaction of the Corporation with or into another corporation, entity or person, other than a transaction in which the holders of at least a majority of the shares of voting capital stock of the Corporation outstanding immediately prior to such transaction continue to hold (either by such shares remaining outstanding or by their being converted into shares of voting capital stock of the surviving entity) a majority of the total voting power represented by the shares of voting capital stock of the Corporation (or surviving entity) outstanding immediately after such transaction, or

(iii) all or substantially all of the Corporation's assets are sold.

D. "Code" means the Internal Revenue Code of 1986, as amended.

E. "common stock" means the Corporation's common stock, \$0.001 par value per share.

F. "Compensation Committee" means a committee of the Board comprised solely of two or more Eligible Directors who are appointed by the Board to administer the Discretionary Grant and Stock Issuance Programs, who are "outside directors" within the meaning of Section 162(m) of the Code and who are "non-employee directors" within the meaning of Rule 16b-3(b)(3)(i).

G. "Consultant" means a consultant or other independent advisor who is under written contract with the Corporation (or any Parent or Subsidiary) to provide consulting or advisory services to the Corporation (or any Parent or Subsidiary) and whose securities issued pursuant to the Plan could be registered on Form S-8.

H. "Corporation" means Pacific Ethanol, Inc., a Delaware corporation, and any corporate successor to all or substantially all of the assets or voting stock of Pacific Ethanol, Inc. that shall by appropriate action adopt the Plan.

I. "Discretionary Grant Program" means the discretionary grant program in effect under Article Two of the Plan pursuant to which stock options and stock appreciation rights may be granted to one or more eligible individuals.

J. “Eligible Director” means a Board member who is not, at the time of such determination, an employee of the Corporation (or any Parent or Subsidiary).

K. “Employee” means an individual who is in the employ of the Corporation (or any Parent or Subsidiary), subject to the control and direction of the employer entity as to both the work to be performed and the manner and method of performance.

L. “Exercise Date” means the date on which the Corporation shall have received written notice of the option exercise.

M. “Fair Market Value” per share of common stock on any relevant date shall be determined in accordance with the following provisions:

(i) If the common stock is at the time traded on The NASDAQ Capital Market, then the Fair Market Value shall be the closing selling price per share of common stock at the close of regular hours trading (i.e., before after-hours trading begins) on The NASDAQ Capital Market on the date in question, as such price is reported by the National Association of Securities Dealers. If there is no closing selling price for the common stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(ii) If the common stock is not traded on The NASDAQ Capital Market but is at the time listed or quoted on any other market or exchange, then the Fair Market Value shall be the closing selling price per share of common stock at the close of regular hours trading (i.e., before after-hours trading begins) on the date in question on the market or exchange determined by the Plan Administrator to be the primary market for the common stock, as such price is officially quoted in the composite tape of transactions on such exchange. If there is no closing selling price for the common stock on the date in question, then the Fair Market Value shall be the closing selling price on the last preceding date for which such quotation exists.

(iii) In the absence of an established market for the common stock, the Fair Market Value shall be determined in good faith by the Plan Administrator.

In addition, with respect to any Incentive Option, the Fair Market Value shall be determined in a manner consistent with any regulations issued by the Secretary of the Treasury for the purpose of determining fair market value of securities subject to an Incentive Option plan under the Code.

N. “Family Member” means, with respect to a particular Optionee or Participant, any child, stepchild, grandchild, parent, stepparent, grandparent, spouse, former spouse, sibling, niece, nephew, mother-in-law, father-in-law, son-in-law, daughter-in-law, brother-in-law or sister-in-law, including adoptive relationships.

O. “Hostile Take-Over” means either of the following events effecting a change in control or ownership of the Corporation:

(i) the acquisition, directly or indirectly, by any person or related group of persons (other than the Corporation or a person that directly or indirectly controls, is controlled by, or is under common control with, the Corporation) of beneficial ownership (within the meaning of Rule 13d-3 of the 1934 Act) of securities possessing more than 50% of the total combined voting power of the Corporation’s outstanding securities pursuant to a tender or exchange offer made directly to the Corporation’s stockholders that the Board does not recommend such stockholders to accept, or

(ii) a change in the composition of the Board over a period of 36 consecutive months or less such that a majority of the Board members ceases, by reason of one or more contested elections for Board membership, to be composed of individuals who either (A) have been Board members continuously since the beginning of such period or (B) have been elected or nominated for election as Board members during such period by at least a majority of the Board members described in clause (A) who were still in office at the time the Board approved such election or nomination.

P. "Incentive Option" means an option that satisfies the requirements of Code Section 422.

Q. "Involuntary Termination" means the termination of the Service of any individual that occurs by reason of:

(i) if such individual is providing services to the Corporation pursuant to a written contract that defines "cause" or "misconduct" or similar reasons such individual could be dismissed or discharged by the Corporation, then such individual's involuntary dismissal or discharge by the Corporation other than for any of such reasons and other than for Misconduct shall be an Involuntary Termination;

(ii) if such individual is not providing services to the Corporation pursuant to a written contract that defines "cause" or "misconduct" or similar reasons such individual could be dismissed or discharged by the Corporation, then such individual's involuntary dismissal or discharge by the Corporation for reasons other than Misconduct shall be an Involuntary Termination;

(iii) if such individual is providing services to the Corporation pursuant to a written contract that defines "good reason" or similar reasons such individual could voluntarily resign, then such individual's voluntary resignation for any of such reasons shall be an Involuntary Termination; or

(iv) if such individual is providing services to the Corporation pursuant to a written contract that does not define "good reason" or similar reasons such individual could voluntarily resign, then such individual's voluntary resignation following (A) a change in his or her position with the Corporation that materially reduces his or her duties and responsibilities or the level of management to which he or she reports, (B) a reduction in his or her level of compensation (including base salary, fringe benefits and target bonus under any corporate-performance based bonus or incentive programs) by more than 15% or (C) a relocation of such individual's place of employment by more than 50 miles, provided and only if such change, reduction or relocation is effected by the Corporation without the individual's consent, shall be an Involuntary Termination.

R. "Misconduct" means the commission of: any act of fraud, embezzlement or dishonesty by the Optionee or Participant; any unauthorized use or disclosure by such person of confidential information or trade secrets of the Corporation (or any Parent or Subsidiary); any illegal or improper conduct or intentional misconduct, gross negligence or recklessness by such person that has adversely affected or, in the determination of the Plan Administrator, is likely to adversely affect, the business, reputation, goodwill or affairs of the Corporation (or any Parent or Subsidiary) in a material manner; any conduct that provides a basis for the Corporation to terminate for "cause," "misconduct" or similar reasons the written contract pursuant to which the Optionee or Participant is providing Services to the Corporation; resignation by the Optionee or Participant on fewer than 30 days' prior written notice and in violation of an agreement to remain in Service of the Corporation, in anticipation of a termination for "cause," "misconduct" or similar reasons under the agreement, or in lieu of a formal discharge for "cause," "misconduct" or similar reasons. The foregoing definition shall not in any way preclude or restrict the right of the Corporation (or any Parent or Subsidiary) to discharge or dismiss any Optionee, Participant or other person in the Service of the Corporation (or any Parent or Subsidiary) for any other acts or omissions, but such other acts or omissions shall not be deemed, for purposes of the Plan, to constitute grounds for termination for Misconduct.

S. “1934 Act” means the Securities Exchange Act of 1934, as amended.

T. “Non-Statutory Option” means an option not intended to satisfy the requirements of Code Section 422.

U. “Optionee” means any person to whom an option is granted under the Discretionary Grant Program.

V. “Parent” means any corporation (other than the Corporation) in an unbroken chain of corporations ending with the Corporation, provided each corporation in the unbroken chain (other than the Corporation) owns, at the time of the determination, stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

W. “Participant” means any person who is issued shares of common stock or restricted stock units or other stock-based awards under the Stock Issuance Program.

X. “Permanent Disability” or “Permanently Disabled” means the inability of the Optionee or the Participant to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment expected to result in death or to be of continuous duration of twelve months or more.

Y. “Plan” means the Corporation’s 2016 Stock Incentive Plan, as set forth in this document.

Z. “Plan Administrator” means the particular entity, whether the Compensation Committee or the Board, which is authorized to administer the Discretionary Grant and Stock Issuance Programs with respect to one or more classes of eligible persons, to the extent such entity is carrying out its administrative functions under those programs with respect to the persons then subject to its jurisdiction.

AA. “Plan Effective Date” means the date that stockholder approval of the Plan is obtained in accordance with Section III.A. of Article Four.

BB. “Section 16 Insider” means an officer or director of the Corporation subject to the short-swing profit liability provisions of Section 16 of the 1934 Act.

CC. “Service” means the performance of services for the Corporation (or any Parent or Subsidiary) by a person in the capacity of an Employee, an Eligible Director or a Consultant, except to the extent otherwise specifically provided in the documents evidencing the Award made to such person. For purposes of the Plan, an Optionee or Participant shall be deemed to cease Service immediately upon the occurrence of either of the following events: (i) the Optionee or Participant no longer performs services in any of the foregoing capacities for the Corporation or any Parent or Subsidiary or (ii) the entity for which the Optionee or Participant is performing such services ceases to remain a Parent or Subsidiary of the Corporation, even though the Optionee or Participant may subsequently continue to perform services for that entity.

DD. “Stock Issuance Agreement” means the agreement entered into by the Corporation and the Participant at the time of issuance of shares of common stock under the Stock Issuance Program.

EE. "Stock Issuance Program" means the stock issuance program in effect under Article Three of the Plan.

FF. "Subsidiary" means any corporation (other than the Corporation) in an unbroken chain of corporations beginning with the Corporation, provided each corporation (other than the last corporation) in the unbroken chain owns, at the time of the determination, stock possessing 50% or more of the total combined voting power of all classes of stock in one of the other corporations in such chain.

GG. "Take-Over Price" means the greater of (i) the Fair Market Value per share of common stock on the date the option is surrendered to the Corporation in connection with a Hostile Take-Over or, if applicable, (ii) the highest reported price per share of common stock paid by the tender offeror in effecting such Hostile Take-Over through the acquisition of such common stock. However, if the surrendered option is an Incentive Option, the Take-Over Price shall not exceed the clause (i) price per share.

HH. "10% Stockholder" means the owner of stock (as determined under Code Section 424(d)) possessing more than 10% of the total combined voting power of all classes of stock of the Corporation (or any Parent or Subsidiary).

II. "Withholding Taxes" means the federal, state and local income and employment taxes to which the Optionee or Participant may become subject in connection with the issuance, exercise or vesting of the Award made to him or her under the Plan.

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Neil M. Koehler, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pacific Ethanol, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2016

/S/ NEIL M. KOEHLER

Neil M. Koehler
President and Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Bryon T. McGregor, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Pacific Ethanol, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

(a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

(b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

(c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

(d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

(a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 9, 2016

/s/ BRYON T. MCGREGOR

Bryon T. McGregor
Chief Financial Officer
(Principal Financial Officer)

**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**

In connection with the Quarterly Report on Form 10-Q of Pacific Ethanol, Inc. (the "Company") for the period ended March 31, 2016 (the "Report"), the undersigned hereby certify in their capacities as Chief Executive Officer and Chief Financial Officer of the Company, respectively, pursuant to 18 U.S.C. section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
2. the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 9, 2016

By: /S/ NEIL M. KOEHLER

Neil M. Koehler
President and Chief Executive Officer
(Principal Executive Officer)

Dated: May 9, 2016

By: /S/ BRYON T. MCGREGOR

Bryon T. McGregor
Chief Financial Officer
(Principal Financial Officer)

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signatures that appear in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.
