Inogen Inc
Form 10-Q
August 11, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2015

OR

¨ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Transition Period From to

Commission file number: 001-36309

INOGEN, INC.

(Exact name of registrant as specified in its charter)

Delaware	33-0989359
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
326 Bollay Drive Goleta, California	93117

(Address of principal executive offices) (Zip Code)
(805) 562-0500

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

Large accelerated filer ¨	Accelerated filer ¨	Non-accelerated filer x	Smaller reporting company ¨ (Do not check if a 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 o No x

As of July 31, 2015, the registrant had 19,347,033 shares of common stock, par value $0.001, outstanding.

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INOGEN, INC.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements.

Inogen, Inc.

Balance Sheets

(unaudited)

(amounts in thousands)

	June 30, 2015	December 31, 2014
Assets		
Current assets		
Cash and cash equivalents	$51,822	$56,836
Short-term investments	14,240	—
Accounts receivable, net of allowances of $6,299 and $3,745 as of June 30, 2015 and December 31, 2014, respectively	24,765	19,349
Inventories, net of allowances of $168 and $141 as of June 30, 2015 and December 31, 2014, respectively	9,308	7,616
Deferred cost of revenue	460	515
Income tax receivable	2,148	2,129
Deferred tax asset - current	4,976	4,976
Prepaid expenses and other current assets	1,723	1,122
Total current assets	109,442	92,543
Property and equipment		
Rental equipment, net of allowances of $932 and $832 as of June 30, 2015 and December 31, 2014, respectively	52,597	48,359
Manufacturing equipment and tooling	4,271	3,985
Computer equipment and software	4,155	3,699
Furniture and equipment	778	649
Leasehold improvements	933	756
Land and building	126	126
Construction in process	400	193
Total property and equipment	63,260	57,767
Less accumulated depreciation	(31,086)	(25,840)
Property and equipment, net	32,174	31,927
Intangible assets, net	238	270

Deferred tax asset - noncurrent	15,248	15,248
Other assets	97	97
Total assets	$157,199	$140,085

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Balance Sheets (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

	June 30, 2015	December 31, 2014
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable and accrued expenses	$17,181	$11,273
Accrued payroll	4,257	4,066
Current portion of long-term debt	307	299
Warranty reserve - current	1,065	781
Deferred revenue - current	2,278	2,316
Total current liabilities	25,088	18,735
Long-term liabilities		
Warranty reserve - noncurrent	541	334
Deferred revenue - noncurrent	3,155	2,176
Long-term debt, net of current portion	159	315
Other noncurrent liabilities	339	375
Total liabilities	29,282	21,935
Commitments and contingencies (Note 5)		
Stockholders' equity		
Common stock, $0.001 par value per share; 200,000,000 authorized; 19,346,143 and 19,059,364 shares issued and outstanding as of June 30, 2015 and December 31, 2014, respectively	19	19
Additional paid-in capital	179,560	174,824
Accumulated deficit	(51,662)	(56,693)
Total stockholders' equity	127,917	118,150
Total liabilities and stockholders' equity	$157,199	$140,085

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Operations

(unaudited)

(amounts in thousands, except share and per share amounts)

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Revenue				
Sales revenue	$32,385	$20,464	$55,434	$35,321
Rental revenue	11,644	9,929	22,347	18,705
Total revenue	44,029	30,393	77,781	54,026
Cost of revenue				
Cost of sales revenue	17,866	10,682	30,455	18,223
Cost of rental revenue, including depreciation of $2,944 and $2,503 for the three months ended and $5,900 and $4,760 for the six months ended, respectively	5,341	4,597	10,481	8,751
Total cost of revenue	23,207	15,279	40,936	26,974
Gross profit				
Gross profit-sales revenue	14,519	9,782	24,979	17,098
Gross profit-rental revenue	6,303	5,332	11,866	9,954
Total gross profit	20,822	15,114	36,845	27,052
Operating expense				
Research and development	975	879	1,838	1,514
Sales and marketing	7,567	6,364	14,491	12,069
General and administrative	6,935	3,908	12,653	7,957
Total operating expense	15,477	11,151	28,982	21,540
Income from operations	5,345	3,963	7,863	5,512
Other income (expense)				
Interest expense	(6)	(203)	(13)	(336)
Interest income	26	12	38	18
Change in fair value of preferred stock warrant liability	—	—	—	36
Other income (expense)	(51)	4	(156)	11
Total other expense, net	(31)	(187)	(131)	(271)
Income before provision for income taxes	5,314	3,776	7,732	5,241
Provision for income taxes	1,855	1,490	2,701	2,067
Net income	$3,459	$2,286	$5,031	$3,174
Basic net income per share attributable to common stockholders (Note 2)	$0.18	$0.13	$0.26	$0.13
Diluted net income per share attributable to common stockholders (Note 2)	$0.17	$0.11	$0.24	$0.11

Weighted-average number of shares used in calculating net income per share attributable to common stockholders:				
Basic common shares	19,310,064	18,201,661	19,239,218	13,843,803
Diluted common shares	20,672,414	20,146,915	20,617,342	15,826,754

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statement of Stockholders' Equity

(unaudited)

(amounts in thousands, except share amounts)

	Common stock		Additional paid-in	Accumulated	Total stockholders'
	Shares	Amount	capital	deficit	equity
Balance, December 31, 2014	19,059,364	$ 19	$ 174,824	$ (56,693)	$ 118,150
Stock-based compensation	—	—	1,327	—	1,327
Employee stock purchase	18,551	—	342	—	342
Excess tax benefits from stock-based compensation arrangements	—	—	2,688	—	2,688
Stock options exercised	268,228	—	379	—	379
Net income	—	—	—	5,031	5,031
Balance, June 30, 2015	19,346,143	$ 19	$ 179,560	$ (51,662)	$ 127,917

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows

(unaudited)

(amounts in thousands)

	Six months ended June 30,	
	2015	2014
Cash flows from operating activities		
Net income	$5,031	$3,174
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,908	5,586
Loss on rental units and other fixed assets	648	921
Provision for sales returns	1,291	1,178
Provision for doubtful accounts	1,118	571
Provision for rental revenue adjustments	4,286	3,411
Provision for inventory obsolescence	53	79
Provision for other inventory losses	60	—
Stock-based compensation expense	1,327	666
Decrease in fair value of preferred stock warrant liability	—	(36)
Deferred tax assets	—	(284)
Excess tax benefits from stock-based compensation arrangements	(2,688)	—
Changes in operating assets and liabilities:		
Accounts receivable	(12,111)	(10,574)
Inventories	(1,805)	(1,932)
Deferred costs of revenue	55	(142)
Income tax receivable	2,669	87
Prepaid expenses and other current assets	(601)	(595)
Accounts payable and accrued expenses	5,923	3,190
Accrued payroll	191	(57)
Warranty reserve	491	269
Deferred revenue	941	1,267
Income tax payable	—	1,435
Other noncurrent liabilities	(36)	(54)
Net cash provided by operating activities	$13,751	$8,160
Cash flows from investing activities		
Purchases of available-for-sale investments	(20,557)	—
Maturities of available-for-sale investments	6,317	—
Investment in intangible assets	(11)	(180)
Production and purchase of rental equipment	(6,485)	(6,752)
Purchases of property and equipment	(1,275)	(603)
Net cash used in investing activities	$(22,011)	$(7,535)

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Inogen, Inc.

Statements of Cash Flows (continued)

(unaudited)

(amounts in thousands)

	Six months ended June 30,	
Cash flows from financing activities	2015	2014
Proceeds from borrowings	—	6,000
Proceeds from redeemable convertible preferred stock warrants and common stock warrants exercised	—	467
Proceeds from stock options exercised	379	109
Proceeds from initial public offering	—	56,471
Costs associated with initial public offering	—	(4,911)
Proceeds from employee stock purchase	342	—
Repayment of debt from investment in intangible assets	(163)	(86)
Repayment of borrowings	—	(3,150)
Excess tax benefits from stock-based compensation arrangements	2,688	—
Net cash provided by financing activities	$3,246	$54,900
Net increase (decrease) in cash and cash equivalents	(5,014)	55,525
Cash and cash equivalents, beginning of period	56,836	13,521
Cash and cash equivalents, end of period	$51,822	$69,046
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	15	317
Cash paid during the period for income taxes, net of refunds received	33	802
Non-cash transactions:		
Deemed dividend on redeemable convertible preferred stock	—	987

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Condensed Notes to the Financial Statements

(unaudited)

(amounts in thousands, except share and per share amounts)

1. General

a) Basis of presentation
The unaudited financial statements have been prepared on the same basis as the annual audited financial statements and, in the opinion of management, reflect all adjustments necessary for a fair presentation for each of the periods presented. The results of operations for interim periods are not necessarily indicative of results to be achieved for full fiscal years or other interim periods.

Inogen, Inc. (Company or Inogen) was incorporated in Delaware on November 27, 2001. The Company is a medical technology company that primarily develops, manufactures and markets innovative portable oxygen concentrators used to deliver supplemental long-term oxygen therapy to patients suffering from chronic respiratory conditions. Traditionally, these patients have relied on stationary oxygen concentrator systems for use in the home and oxygen tanks or cylinders for mobile use, which the Company calls the delivery model. The tanks and cylinders must be delivered regularly and have a finite amount of oxygen, which requires patients to plan activities outside of their homes around delivery schedules and a finite oxygen supply. Additionally, patients must attach long, cumbersome tubing to their stationary concentrators simply to enable mobility within their homes. The Company's proprietary Inogen One® systems concentrate the air around the patient to offer a single source of supplemental oxygen anytime, anywhere with a portable device weighing approximately 4.8 or 7.0 pounds. The Company's Inogen One G2® and Inogen One G3™ have up to 5 and 4.5 hours of battery life, respectively, with a single battery and can be plugged into an outlet when at home, in a car, or in a public place with outlets available. The Company's Inogen One systems reduce the patient's reliance on stationary concentrators and scheduled deliveries of tanks with a finite supply of oxygen, thereby improving patient quality of life and fostering mobility.

Although portable oxygen concentrators represent the fastest-growing segment of the Medicare oxygen therapy market, the Company estimates based on 2013 Medicare data that patients using portable oxygen concentrators represent approximately 5% to 7% of the total addressable oxygen market in the United States. Based on 2013 industry data, the Company believes it was the leading worldwide manufacturer of portable oxygen concentrators, as well as the largest provider of portable oxygen concentrators to Medicare patients, as measured by dollar volume. The Company believes it is the only manufacturer of portable oxygen concentrators that employs a direct-to-consumer strategy in the United States, meaning the Company markets its products to patients, processes their physician paperwork, provides clinical support as needed and bills Medicare or insurance on their behalf. To pursue a direct-to-consumer strategy, the Company's manufacturing competitors would need to meet national accreditation and state-by-state licensing requirements and secure Medicare billing privileges, as well as compete with the home medical equipment providers that many rely on across their entire homecare business.

Since adopting the Company's direct-to-consumer strategy in 2009 following its acquisition of Comfort Life Medical Supply, LLC, which had an active Medicare billing number but few other assets and limited business activities, the Company has directly sold or rented its Inogen One systems to more than 97,000 patients as of June 30, 2015. Revenue has grown from $10,700 in 2009 to $112,500 in 2014.

As contemplated by the Securities and Exchange Commission (SEC) under Rule 10-01 of Regulation S-X, the accompanying financial statements and related footnotes have been condensed and do not contain certain information that will be included in the Company's annual financial statements and footnotes thereto. For further information refer to the financial statements and related footnotes included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014 filed with the SEC on April 27, 2015 (Annual Report).

b) Use of estimates

The preparation of the Company's financial statements in accordance with generally accepted accounting principles in the United States (GAAP) requires management to make estimates and assumptions that affect the amounts reported in these financial statements and accompanying condensed notes. Management bases these estimates and assumptions upon historical experience, existing and known circumstances, authoritative accounting pronouncements and other factors that management believes to be reasonable. Significant areas requiring the use of management estimates relate to inventory and rental asset valuations and write-downs, accounts receivable reserves and allowance for bad debts, returns and adjustments, stock compensation expense, impairment assessments, depreciation and amortization, income tax provision and uncertain tax positions, fair value of financial instruments, and fair values of acquired intangibles. Actual results could differ materially from these estimates.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

c) Reclassifications
Certain reclassifications have been made to prior years' financial statements to conform to current period financial statements' presentation with no effect on previously reported financial position, results of operations or cash flows. These changes consisted of reclassifications to certain line items in the accompanying Statements of Operations and Statements of Cash Flows.

d) Initial public offering (IPO)
The Company completed an initial public offering on February 20, 2014, and sold 3,529,411 shares to the public for $16.00 per share. In addition, the selling stockholders sold 981,902 shares for a combined total of 4,511,313 shares sold in the offering. The Company netted approximately $49,668 after the underwriters' discount and other associated expenses. In connection with the completion of the Company's IPO, the Company's 9,546,140 shares of redeemable convertible preferred stock and 66,666 shares of convertible preferred stock were automatically converted into 14,259,647 shares of common stock. Following the IPO, all warrants previously exercisable for preferred stock became exercisable for common stock. The previously reported warrant liability associated with the convertible warrants was applied to additional paid-in capital. During the six months ended June 30, 2014, the Company recognized a partial period deemed dividend of $987 for the time-frame the redeemable convertible preferred stock was outstanding during the period. The Company had no redeemable convertible preferred stock or convertible preferred stock outstanding as of December 31, 2014 or June 30, 2015, respectively. As of June 30, 2015, the Company had 19,346,143 shares of common stock outstanding.

e) Recent Accounting Pronouncements
Revenue Recognition: In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update No. 2014-09 (ASU 2014-09), Revenue from Contracts with Customers (Topic 606). The update supersedes nearly all existing revenue recognition guidance under GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled to those goods or services. ASU 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing GAAP.

Subsequent to June 30, 2015, the FASB decided to delay the effective date of ASU 2014-09 by one year. The FASB also agreed to allow entities to choose to adopt the standard as of the original effective date. As such, the updated standard will be effective for us in the first quarter of 2018, with the option to adopt t in the first quarter of 2017. The Company is currently evaluating the impact of the Company's pending adoption of ASU 2014-09 on the Company's financial statements and has not yet determined the method by which the Company will adopt the standard.

Interest: In April 2015, the FASB issued ASU 2015-03, Interest - Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs. The update requires that debt issuance costs related to a recognized debt liability be presented in the balance sheet as a direct deduction from the carrying amount of that debt liability, consistent with debt discounts. This update is effective for our fiscal year beginning January 1, 2016 with

early adoption permitted. The adoption of this standard is not expected to have a material effect on our financial condition, results of operations or cash flows.

Intangibles - Goodwill and Other - Internal Use Software: In April 2015, the FASB issued ASU 2015-05, Intangibles-Goodwill and Other-Internal Use Software - Customer's Accounting for Fees Paid in a Cloud Computing Arrangement. The update provides guidance on fees paid by an entity in a cloud computing arrangement and whether an arrangement includes a license to the underlying software. If a cloud computing arrangement includes a software license, then the entity should account for the software license element of the arrangement consistent with the acquisition of other software licenses. If a cloud computing arrangement does not include a software license, the entity should account for the arrangement as a service contract. This update is effective for our fiscal year beginning January 1, 2016. The adoption of this standard is not expected to have a material effect on our financial condition, results of operations or cash flows.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

2. Summary of significant accounting policies

Sales revenue

The Company generates revenue primarily from sales and rentals of its products. The Company's products consist of its proprietary line of oxygen concentrators and related accessories. Other revenue, which is included in sales revenue on the Statements of Operations, comes from service contracts, extended warranty contracts and freight revenue for product shipments.

Revenue from product sales is recognized when all of the following criteria are met: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services have been rendered; (3) the price to the customer is fixed or determinable; and (4) collectability is reasonably assured. Revenue from product sales is generally recognized upon shipment of the product. Provisions for estimated returns and discounts are made at the time revenue is recognized. Provisions for standard warranty obligations, which are included in cost of sales revenue on the Statements of Operations, are also provided for at the time revenue is recognized.

Revenue from the sale of the Company's services is recognized when no significant obligations remain undelivered and collection of the receivables is reasonably assured. The Company offers extended service contracts on its Inogen One concentrator line for periods ranging from 12 to 24 months after the end of the standard warranty period. Revenue from these extended service contracts is recognized in income on a straight-line basis over the contract period.

Accruals for estimated standard warranty expenses are made at the time that the associated revenue is recognized. The provisions for estimated returns, discounts and warranty obligations are made based on known claims and discount commitments and estimates of additional returns and warranty obligations based on historical data and future expectations. The Company's accrued warranty liability was $1,606 and $1,115 for future warranty costs as of June 30, 2015 and December 31, 2014, respectively.

The Company also offers a lifetime warranty for direct-to-consumer sales. For a fixed price, the Company agrees to provide a fully functional oxygen concentrator for the remaining life of the patient. Lifetime warranties are only offered to patients upon the initial sale of oxygen equipment by the Company and are non-transferable. Product sales with lifetime warranties are considered to be multiple element arrangements within the scope of the Accounting Standards Codification (ASC) 605-25—Revenue Recognition-Multiple-Element Arrangements.

There are two deliverables when a product that includes a lifetime warranty is sold. The first deliverable is the oxygen concentrator equipment which comes with a standard warranty of three years. The second deliverable is the lifetime warranty that provides for a functional oxygen concentrator for the remaining lifetime of the patient. These two deliverables qualify as separate units of accounting.

The revenue is allocated to the two deliverables on a relative selling price method. The Company has vendor-specific objective evidence of selling price for the equipment. To determine the selling price of the lifetime warranty, the Company uses its best estimate of the selling price for that deliverable as the lifetime warranty is neither separately priced nor is the selling price available through third-party evidence. To calculate the selling price associated with the lifetime warranties, management considered the profit margins of the overall business, the average estimated cost of lifetime warranties and the price of extended warranties. A significant estimate used to calculate the price and expense of lifetime warranties is the life expectancy of patients. Based on clinical studies, the Company estimates that 60% of patients will succumb to their disease within three years. Given the approximate mortality rate of 20% per year, the Company estimates on average all patients will succumb to their disease within five years. The Company has taken into consideration that when patients decide to buy an Inogen portable oxygen concentrator with a lifetime warranty, they typically have already been on oxygen for a period of time, which can have a large impact on their life expectancy from the time the Company's product is deployed.

After applying the relative selling price method, revenue from equipment sales is recognized when all other revenue recognition criteria for product sales are met. Lifetime warranty revenue is recognized using the straight-line method during the fourth and fifth year after the delivery of the equipment which is the estimated usage period of the contract based on the average patient life expectancy.

Shipping and handling costs for sold products and rental assets shipped to the Company's customers are included on the Statements of Operations as part of cost of sales revenue and cost of rental revenue, respectively.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

Revenue from the sales of used rental equipment is recognized upon shipment and when collectability is reasonably assured and other revenue recognition criteria are met. When a rental unit is sold, the related cost and accumulated depreciation are removed from their respective accounts, and any gains or losses are included in cost of sales revenue on the Statements of Operations.

Rental revenue

The Company recognizes equipment rental revenue over the non-cancelable lease term, which is one month, less estimated adjustments, in accordance with ASC 840—Leases. The Company has separate contracts with each patient that are not subject to a master lease agreement with any payor. The Company evaluates the individual lease contracts at lease inception and the start of each monthly renewal period to determine if there is reasonable assurance that the bargain renewal option associated with the potential capped free rental period would be exercised. Historically, the exercise of such bargain renewal option is not reasonably assured at lease inception and most subsequent monthly lease renewal periods. If the Company determines that the reasonable assurance threshold for an individual patient is met at lease inception or at a monthly lease renewal period, such determination would impact the bargain renewal period for an individual lease. The Company would first consider the lease classification issue (sales-type lease or operating lease) and then appropriately recognize or defer rental revenue over the lease term, which may include a portion of the capped rental period. To date, the Company has not deferred any amounts associated with the capped rental period. Amounts related to the capped rental period have not been material in the periods presented.

The lease term begins on the date products are shipped to patients and are recorded at amounts estimated to be received under reimbursement arrangements with third-party payors, including Medicare, private payors, and Medicaid. Due to the nature of the industry and the reimbursement environment in which the Company operates, certain estimates are required to record net revenue and accounts receivable at their net realizable values. Inherent in these estimates is the risk that they will have to be revised or updated as additional information becomes available. Specifically, the complexity of many third-party billing arrangements and the uncertainty of reimbursement amounts for certain services from certain payors may result in adjustments to amounts originally recorded. Such adjustments are typically identified and recorded at the point of cash application, claim denial or account review. Accounts receivable are reduced by an allowance for doubtful accounts which provides for those accounts from which payment is not expected to be received although product was delivered and revenue was earned. Upon determination that an account is uncollectible, it is written-off and charged to the allowance. Amounts billed but not earned due to the timing of the billing cycle are deferred and recognized in income on a straight-line basis over the monthly billing period. For example, if the first day of the billing period does not fall on the first of the month, then a portion of the monthly billing period will fall in the subsequent month and the related revenue and cost would be deferred based on the service days in the following month.

Rental revenue is recognized as earned, less estimated adjustments. Revenue not billed at the end of the period is reviewed for the likelihood of collections and accrued. The rental revenue stream is not guaranteed and payment will cease if the patient no longer needs oxygen or returns the equipment. Revenue recognized is at full estimated

allowable amounts; transfers to secondary insurances or patient responsibility have no net effect on revenue. Rental revenue is earned for that month if the patient is on service on the first day of the 30-day period commencing on the recurring date of service for a particular claim, regardless if there is a change in condition or death after that date.

Included in rental revenue are unbilled amounts for which the revenue recognition criteria had been met as of period-end but were not yet billed to the payor. The estimate of unbilled rental revenue is based on historical trends and estimates of future collectability. In addition, the Company estimates potential future adjustments and write-offs of these unbilled amounts and includes these estimates in the allowance for adjustments and write-offs of rental revenue which is netted against gross receivables.

Fair value of financial instruments

The Company’s financial instruments consist of cash and cash equivalents, short-term investments, accounts receivable, accounts payable and accrued expenses, debt and warrants. The carrying values of cash and cash equivalents, short-term investments, accounts receivable and accounts payable and accrued expenses approximate fair values based on the short-term nature of these financial instruments.

The fair value of the Company’s debt approximates carrying value based on the Company’s current incremental borrowing rate for similar types of borrowing arrangements. Imputed interest associated with the Company’s non-interest bearing debt is insignificant and has been appropriately recognized in the respective periods.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

Fair value accounting

ASC 820—Fair Value Measurements and Disclosures, creates a single definition of fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements. ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement should be determined based on assumptions that market participants would use in pricing the asset or liability. Assets and liabilities adjusted to fair value in the balance sheet are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Level inputs, as defined by ASC 820, are as follows:

Level input	Input definition
Level 1	Inputs are unadjusted, quoted prices for identical assets or liabilities in active markets at the measurement date.
Level 2	Inputs, other than quoted prices included in Level 1 that are observable for the asset or liability through corroboration with market data at the measurement date.
Level 3	Unobservable inputs that reflect management’s best estimate of what market participants would use in pricing the asset or liability at the measurement date.

The Company obtained the fair value of its available-for-sale securities, which are not in active markets, from a third-party professional pricing service using quoted market prices for identical or comparable instruments, rather than direct observations of quoted prices in active markets. The Company's professional pricing service gathers observable inputs for all of its fixed income securities from a variety of industry data providers (e.g., large custodial institutions) and other third-party sources. Once the observable inputs are gathered, all data points are considered and the fair value is determined. The Company validates the quoted market prices provided by its primary pricing service by comparing their assessment of the fair values against the fair values provided by its investment managers. The Company's investment managers use similar techniques to its professional pricing service to derive pricing as described above. As all significant inputs were observable, derived from observable information in the marketplace or supported by observable levels at which transactions are executed in the marketplace, the Company has classified its available-for-sale securities within Level 2 of the fair value hierarchy.

The following table summarizes fair value measurements by level for the assets measured at fair value on a recurring basis:

As of December 31, 2014	Level 2	Total

	Level 1		Level 3	
Certificates of deposit	$ —	$11,633	$ —	$11,633
Total assets	$ —	$11,633	$ —	$11,633

As of June 30, 2015	Level 1	Level 2	Level 3	Total
Certificates of deposit	$ —	$23,587	$ —	$23,587
Total assets	$ —	$23,587	$ —	$23,587

Cash Equivalents

The Company considers all short-term highly liquid investments with a maturity of three months or less to be cash equivalents. Cash equivalents primarily consist of funds held in money market accounts, which were $10,100 and $42,300 as of June 30, 2015 and December 31, 2014, respectively. Cash equivalents are recorded at cost plus accrued interest, which approximates fair value. Certificates of deposit are included in cash equivalents and short-term investments based on the maturity date of the security.

Investments

The Company considers investments with maturities greater than three months, but less than one year, to be short-term investments. Investments that have maturities of more than one year are classified as long-term investments. Investments are classified as available-for-sale and are reported at fair value with unrealized gains or losses, if any, reported, net of tax, in accumulated other comprehensive income. The fair value measurement of the investments had an immaterial impact on Other Comprehensive Income. The Company does not have any other items which would be classified within Other Comprehensive Income. Therefore, there would be no change between the reported Net Income and Other Comprehensive Income due to the immateriality of the unrealized gains or losses

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associated with investments. The cost of investments sold is based on the specific identification method, and all income generated and realized gains or losses from investments are recorded to interest and other income (expense), net.

The Company reviews its investments to identify and evaluate investments that have an indication of possible impairment. Factors considered in determining whether a loss is temporary include the length of time and extent to which fair value has been less than the cost basis, the financial condition and near-term prospects of the investee, and the Company's intent and ability to hold the investment for a period of time sufficient to allow for any anticipated recovery in market value. Credit losses and other-than-temporary impairments are declines in fair value that are not expected to recover and are charged to interest and other income (expense), net.

Accounts receivable and allowance for bad debts, returns, and adjustments

Accounts receivable are customer obligations due under normal sales and rental terms. The Company performs credit evaluations of the customers' financial condition and generally does not require collateral. The allowance for doubtful accounts is maintained at a level that, in management's opinion, is adequate to absorb potential losses related to accounts receivable and is based upon the Company's continuous evaluation of the collectability of outstanding balances. Management's evaluation takes into consideration such factors as past bad debt experience, economic conditions and information about specific receivables. The Company's evaluation also considers the age and composition of the outstanding amounts in determining their net realizable value.

The allowance is based on estimates, and ultimate losses may vary from current estimates. As adjustments to these estimates become necessary, they are reported in earnings in the periods that they become known. The allowance is increased by bad debt provisions charged to bad debt expense, net of recoveries, in operating expense and is reduced by direct write-offs, net of recoveries.

The Company generally does not allow returns from providers for reasons not covered under its standard warranty. Therefore, provision for sales returns applies to direct-to-consumer sales only. This reserve is calculated based on actual historical return rates under the Company's 30-day return program and is applied to the sales revenue for direct-to-consumer sales for the last month of the quarter reported.

The Company also records an allowance for rental revenue adjustments and write-offs, which is recorded as a reduction of rental revenue and rental accounts receivable balances. These adjustments and write-offs result from contractual adjustments, audit adjustments, untimely claims filings or billings not paid due to another provider performing same or similar functions for the patient in the same period, all of which prevent billed revenue from becoming realizable. The reserve is based on historical revenue adjustments as a percentage of rental revenue billed and rental revenue unbilled during the related period.

When recording the allowance for doubtful accounts, the bad debt expense account (general and administrative expense account) is charged; when recording allowance for sales returns, the sales returns account (contra sales revenue account) is charged; and when recording the allowance for adjustments, the rental revenue adjustments account (contra rental revenue account) is charged.

As of June 30, 2015 and December 31, 2014, included in accounts receivable on the balance sheets were earned but unbilled receivables of $4,141 and $3,653, respectively. These balances reflect gross unbilled receivables prior to any allowances for adjustments and write-offs.

Concentration of credit risk

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of cash and cash equivalents and accounts receivable. At times, cash account balances may be in excess of the amounts insured by the Federal Deposit Insurance Corporation (FDIC). However, management believes the risk of loss to be minimal. The Company performs periodic evaluations of the relative credit standing of these institutions and has not experienced any losses on its cash and cash equivalents to date.

Concentration of customers and vendors

The Company sells its products to home medical equipment providers, distributors, and resellers in the United States and in foreign countries on a credit basis. The Company sells its products to consumers on a prepayment basis. No single customer represented more

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than 10% of the Company's total revenue for the six months ended June 30, 2015 and June 30, 2014. No single customer represented more than 10% of the Company's total accounts receivable balance as of June 30, 2015, or as of December 31, 2014.

The Company also rents products directly to consumers for insurance reimbursement, which resulted in a customer concentration relating to Medicare's service reimbursement programs. Medicare's service reimbursement programs accounted for 73.1% and 71.7% of rental revenue for the three months ended June 30, 2015 and June 30, 2014, respectively, and based on total revenue were 19.3% and 23.4% for the three months ended June 30, 2015 and June 30, 2014, respectively. Medicare's service reimbursement programs accounted for 72.9% and 72.1% of rental revenue for the six months ended June 30, 2015 and June 30, 2014, respectively, and based on total revenue were 21.0% and 25.0% for the six months ended June 30, 2015 and June 30, 2014, respectively. Accounts receivable balances relating to Medicare's service reimbursement programs amounted to $7,488 or 30.2% of total accounts receivable as of June 30, 2015 as compared to $4,875, or 25.2% of total accounts receivable as of December 31, 2014.

The Company currently purchases raw materials from a limited number of vendors, which resulted in a concentration of three major vendors. The three major vendors supply the Company with raw materials used to manufacture the Company's products. For the six months ended June 30, 2015, the Company's three major vendors accounted for 21.6%, 17.7%, and 9.6%, respectively, of total raw material purchases. For the six months ended June 30, 2014, the Company's three major vendors accounted for 22.6%, 18.1% and 8.5%, respectively, of total raw material purchases.

A portion of revenue is earned from sales outside the United States. Approximately 70% of the non-U.S. revenue for the three months and six months ended June 30, 2015 was invoiced in euros. We did not begin to invoice in euros until the fourth quarter of 2014. A breakdown of the Company's revenue from U.S. and non-U.S. sources for the three months and six months ended June 30, 2015 and June 30, 2014 is as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
U.S. revenue	$33,458	$24,237	$58,812	$43,424
Non-U.S. revenue	10,571	6,156	18,969	10,602
Total revenue	$44,029	$30,393	$77,781	$54,026

Inventories

Inventories are stated at the lower of cost or market. Cost is determined using a standard cost method, including material, labor and manufacturing overhead, whereby the standard costs are updated at least quarterly to reflect approximate actual costs using the first-in, first out (FIFO) method and market represents the lower of replacement cost or estimated net realizable value. The Company records adjustments at least quarterly to inventory for potentially excess, obsolete, slow-moving or impaired items. Inventories consist of the following:

	June 30, 2015	December 31, 2014
Raw materials and work-in-progress	$8,118	$ 6,774
Finished goods	1,358	983
Less: reserves	(168)	(141)
Inventories	$9,308	$ 7,616

Property and equipment

Property and equipment are stated at cost. Depreciation and amortization are calculated using the straight-line method over the assets' estimated useful lives as follows:

Rental equipment	1.5-5 years
Manufacturing equipment and tooling	5 years
Computer equipment and software	3 years
Furniture and equipment	3-5 years
Leasehold improvements	Shorter of 3-10 years or life of underlying lease

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Expenditures for additions, improvements and replacements are capitalized and depreciated to a salvage value of zero. Repair and maintenance costs are included in cost of revenue on the Statements of Operations. Repair and maintenance expense, which includes labor, parts and freight for rental equipment was $642 and $400 for the three months ended June 30, 2015 and June 30, 2014, respectively, and $1,212 and $790 for the six months ended June 30, 2015 and June 30, 2014, respectively.

Included within property and equipment is construction in process relating to the design and engineering of tooling, jigs and other machinery. In addition, this item also includes computer software that has been purchased, but has not completed the final configuration process for implementation into the Company's systems. These items have not been placed in service; therefore, no depreciation and amortization has been recognized in respective periods.

Depreciation and amortization expense related to property and equipment and rental equipment is summarized below for the three months ended June 30, 2015 and June 30, 2014, respectively, and for the six months ended June 30, 2015 and June 30, 2014, respectively.

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Rental equipment	$2,944	$2,503	$5,900	$4,760
Other property and equipment	498	384	965	746
Total depreciation and amortization	$3,442	$2,887	$6,865	$5,506

Property and equipment and rental equipment with associated accumulated depreciation is summarized below for June 30, 2015 and December 31, 2014, respectively.

Property and equipment	June 30, 2015	December 31, 2014
Rental equipment, net of allowance	$52,597	$ 48,359
Other property and equipment	10,663	9,408
Property and equipment	63,260	57,767

Accumulated depreciation		
Rental equipment	25,383	21,084
Other property and equipment	5,703	4,756
Accumulated depreciation	31,086	25,840
Net property and equipment		
Rental equipment	27,214	27,275
Other property and equipment	4,960	4,652
Property and equipment, net	$32,174	$31,927

Income taxes

The Company accounts for income taxes in accordance with ASC 740—Income Taxes. Under ASC 740, income taxes are recognized for the amount of taxes payable or refundable for the current period and deferred tax liabilities and assets are recognized for the future tax consequences of transactions that have been recognized in the Company's financial statements or tax returns. A valuation allowance is provided when it is more likely than not that some portion, or all, of the deferred tax asset will not be realized.

The Company accounts for uncertainties in income tax in accordance with ASC 740-10—Accounting for Uncertainty in Income Taxes. ASC 740-10 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. This accounting standard also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

The Company recognizes interest and penalties on taxes, if any, within operations as income tax expense. No significant interest or penalties were recognized during the periods presented.

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The Company operates in multiple states. The statute of limitations has expired for all tax years prior to 2011 for federal and 2010 to 2011 for various state tax purposes. However, the net operating loss generated on the federal and state tax returns in prior years may be subject to adjustments by the federal and state tax authorities.

Income tax expense was $1,855 and $2,701, an effective tax rate of 34.9% and 34.9%, for the three and six months ended June 30, 2015, respectively, compared to $1,490 and $2,067, an effective tax rate of 39.5% and 39.4%, for the comparable periods ended June 30, 2014, respectively. Variations in the tax rate year-over-year were primarily due to a decrease in permanent tax differences related to the domestic production activities deduction and the California research and development tax credit.

Accounting for stock-based compensation

The Company accounts for its stock-based compensation in accordance with ASC 718, Compensation—Stock Compensation, which establishes accounting for share-based awards, exchanged for employee services and requires companies to expense the estimated fair value of these awards over the requisite employee service period. Stock–based compensation cost is determined at the grant date using the Black-Scholes option pricing model. The value of the award that is ultimately expected to vest is recognized as expense on a straight-line basis over the employee's requisite service period.

As part of the provisions of ASC 718, the Company is required to estimate potential forfeitures of stock grants and adjust compensation cost recorded accordingly. The estimate of forfeitures will be adjusted over the requisite service period to the extent that actual forfeitures differ, or are expected to differ, from such estimates. Changes in estimated forfeitures will be recognized through a cumulative catch-up adjustment in the period of change and will also impact the amount of stock compensation expense to be recognized in future periods.

Business segments

The Company operates in only one business segment – manufacturing, sales, rental and marketing of respiratory products.

Earnings per share

Earnings per share (EPS) is computed in accordance with ASC 260, Earnings per Share, and is calculated using the weighted-average number of common shares outstanding during each period. Diluted EPS assumes the conversion, exercise or issuance of all potential common stock equivalents (which can include dilution of outstanding stock options and common stock warrants) unless the effect is to reduce a loss or increase the income per share. For purposes of this calculation, common stock subject to repurchase by the Company, options and warrants are

considered to be common stock equivalents and are only included in the calculation of diluted earnings per share when their effect is dilutive.

The shares used to compute basic and diluted net income per share represent the weighted-average common shares outstanding, reduced by the weighted-average unvested common shares subject to repurchase.

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The computation of EPS is as follows:

	Three months ended June 30,		Six months ended June 30,	
	2015	2014	2015	2014
Numerator—basic:				
Net income	$3,459	$2,286	$5,031	$3,174
Less deemed dividend on redeemable convertible preferred stock	—	—	—	(987)
Net income before preferred rights dividend	3,459	2,286	5,031	2,187
Less: undistributed earnings to preferred stock - basic	—	—	—	(438)
Net income attributable to common stockholders - basic	$3,459	$2,286	$5,031	$1,749
Numerator—diluted:				
Net income	$3,459	$2,286	$5,031	$3,174
Less deemed dividend on redeemable convertible preferred stock	—	—	—	(987)
Net income before preferred rights dividend	3,459	2,286	5,031	2,187
Less: undistributed earnings to preferred stock - diluted	—	—	—	(393)
Net income attributable to common stockholders - diluted	$3,459	$2,286	$5,031	$1,794
Denominator:				
Weighted-average common shares - basic common stock	19,310,064	18,201,661	19,239,218	13,843,803
Weighted-average common shares - diluted common stock	20,672,414	20,146,915	20,617,342	15,826,754
Net income per share - basic common stock	$0.18	$0.13	$0.26	$0.13
Net income per share - diluted common stock	$0.17	$0.11	$0.24	$0.11
Shares excluded from diluted net income:				
Stock options	582,970	—	612,970	—
Shares excluded from diluted net income	582,970	—	612,970	—
Denominator calculation from basic to diluted:				
Weighted-average common shares - basic common stock	19,310,064	18,201,661	19,239,218	13,843,803
Warrants	9,663	159,475	9,657	166,455
Stock options	1,352,687	1,785,779	1,368,467	1,816,496
Weighted-average common shares - diluted common stock	20,672,414	20,146,915	20,617,342	15,826,754

The computations of diluted net income attributable to common stockholders exclude common stock options which were anti-dilutive for the three months and six months ended June 30, 2015.

3. Intangible assets

During the year ended December 31, 2008, the Company acquired Comfort Life Medical, LLC. The acquisition resulted in recording an intangible asset in the amount of $92 related to the Medicare license held by the acquired company. The Company amortizes this intangible asset over its estimated useful life of ten years. As of June 30, 2015 and December 31, 2014, there were no impairments recorded related to this intangible asset. On April 1, 2009, Comfort Life Medical, LLC merged with Inogen, Inc., and was simultaneously dissolved. During the year ended December 31, 2009, the Company was assigned four patents previously held as an exclusive license from Air Products & Chemicals (APC) in exchange for an increase in a long-term liability due to APC of $250. The acquisition of these patents resulted in an intangible asset of $250. During the year ended December 31, 2011, the Company purchased additional patents from APC for a total value of $650. The Company amortizes these intangible assets over an estimated useful life of five years. There were no impairments recorded related to these intangible assets during the three months and six months ended June 30, 2015 and June 30, 2014. The Company recalculated interest and amortization during the respective periods based on adjusted asset and debt.

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During the year ended December 31, 2011, the Company acquired Breathe Oxygen Services, LLC. The acquisition resulted in recording an intangible asset in the amount of $66 related to the Medicare license held by the acquired Breathe Oxygen Services that allowed them to operate in the state of Tennessee as well as other assets. On August 29, 2011, Breathe Oxygen Services, LLC merged with Inogen, Inc., and was simultaneously dissolved. The Company amortizes this intangible asset over its estimated useful life of ten years. During the three months and six months ended June 30, 2015 and June 30, 2014, there were no impairments recorded related to this intangible asset.

The Company also capitalizes costs incurred for the production of direct response advertising commercials and amortizes these intangible assets over a useful life of two years. During the six months ended June 30, 2015, the Company paid $11 for its production of commercials. The Company did not capitalize any intangible assets during the three months ended June 30, 2015. During the three months and six months ended June 30, 2014, the Company paid $11 and $180, respectively, for its patient setup video, website development and redesign, and production of commercials.

Amortization expense for intangible assets for the three months ended June 30, 2015 and June 30, 2014 was $22 and $41, respectively, and for the six months ended June 30, 2015 and June 30, 2014 was $43 and $80, respectively.

4. Long-term debt

JP Morgan Chase debt

In November 2014, the Company secured a primary banking relationship that provides access to a $15,000 working capital revolving line of credit, and treasury and cash management services through commercial banking with JP Morgan Chase. This agreement is a three year working capital revolving line of credit which replaces the previous loan facility the Company maintained with Comerica. The interest rate on outstanding debt balances will be the London Interbank Offer Rate (LIBOR) plus 1.25%. The Company is required to maintain a tangible net worth not less than $90,000 and EBITDA of $10,000 for any period of four consecutive quarters commencing with the four-quarter test period ending September 30, 2014. Beginning with the second quarter of 2016, the EBITDA will increase to a $12,500 minimum calculation, of which the Company is currently compliant under either requirement as of June 30, 2015, and no debt balances were outstanding on the credit facility.

June 30, 2015	December 31, 2014

Contractual obligation, bearing imputed interest at prime plus two, quarterly payments of $53 beginning May 2011 through October 2014 and quarterly payments of $81 beginning January 2015 through October 2016	$ 466	$ 614
Less: current maturities	(307)	(299)
Long-term debt, net of current portion	$ 159	$ 315

As of June 30, 2015, the minimum aggregate payments due under non-cancelable debt are summarized as follows:

	June 30, 2015
Remaining 6 months of 2015	$ 151
2016	315
Total	$ 466

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5. Commitments and contingencies

Leases

The Company leases its offices and certain equipment under operating leases that expire through January 2022. As of June 30, 2015, the minimum aggregate payments due under non-cancelable leases are summarized as follows:

	June 30, 2015
Remaining 6 months of 2015	$512
2016	1,041
2017	1,052
2018	1,044
2019	1,057
Thereafter	819
	$5,525

Rent expense of $220 and $180 for the three months ended June 30, 2015 and June 30, 2014, respectively, and $440 and $387 for the six months ended June 30, 2015 and June 30, 2014, respectively, was included in the accompanying Statements of Operations.

Warranty obligation

The following table identifies the changes in the Company’s aggregate product warranty liabilities for the six and twelve month periods ended June 30, 2015 and December 31, 2014, respectively:

	June 30, 2015	December 31, 2014
Product warranty liability at beginning of period	$1,115	$ 809
Accruals for warranties issued	927	1,075
Adjustments related to preexisting warranties (including changes in estimates)	260	406
Settlements made (in cash or in kind)	(696)	(1,175)
Product warranty liability at end of period	$1,606	$ 1,115

Legislation and HIPAA

The healthcare industry is subject to numerous laws and regulations of federal, state and local governments. These laws and regulations include, but are not necessarily limited to, matters such as licensure, accreditation, government healthcare program participation requirements, reimbursement for patient services, and Medicare and Medicaid fraud and abuse. Government activity has continued with respect to investigations and allegations concerning possible violations of fraud and abuse statutes and regulations by healthcare providers. Violations of these laws and regulations could result in expulsion from government healthcare programs together with the imposition of significant fines and penalties, as well as significant repayments for patient services previously billed.

The Company believes that it is in compliance in all material respects with applicable fraud and abuse regulations and other applicable government laws and regulations. Compliance with such laws and regulations can be subject to future government review and interpretation as well as regulatory actions unknown or unasserted at this time. The Company believes that it complies in all material respects with the provisions of those regulations that are applicable to the Company’s business.

The Health Insurance Portability and Accountability Act (HIPAA) assures health insurance portability, reduces healthcare fraud and abuse, guarantees security and privacy of health information, and enforces standards for health information. The Health Information Technology for Economic and Clinical Health Act (HITECH Act) imposes notification requirements of certain security breaches relating to protected health information. The Company may be subject to significant fines and penalties if found not to be compliant with the provisions outlined in the regulations.

Legal proceedings

On November 4, 2011, the Company filed a lawsuit in the United States District Court for the Central District of California against Inova Labs Inc., or Defendant, for infringement of two of the Company’s patents. The case, Inogen Inc. v. Inova Labs Inc., Case No.

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8:11-cv-01692-JST-AN, or the Lawsuit, involves U.S. Patent Nos. 7,841,343, entitled “Systems and Methods For Delivering Therapeutic Gas to Patients”, or the ’343 patent, and 6,605,136 entitled “Pressure Swing Adsorption Process Operation And Optimization”, or the ’136 patent. The Company alleged in the Lawsuit that certain of Defendant’s oxygen concentrators infringe various claims of the ’343 and ’136 patents. The Lawsuit seeks damages, injunctive relief, costs and attorney fees.

The Defendant has answered the complaint, denying infringement and asserting various sets of defenses including non-infringement, invalidity and unenforceability, patent misuse, unclean hands, laches and estoppel. The Defendant also filed counterclaims against us alleging patent invalidity, non-infringement and inequitable conduct. The Company denied the allegations in the Defendant’s counterclaims. The Company has filed a motion to dismiss Defendant’s inequitable conduct counterclaim.

The Defendant filed a request with the U.S. Patent and Trademark Office seeking an inter partes reexamination of the ’343 and ’136 patents. The Defendant also filed a motion to stay the Lawsuit pending outcome of the reexamination. On March 20, 2012, the Court granted the Defendant’s motion to stay the Lawsuit pending outcome of the reexamination and also granted the Company’s motion to dismiss the Defendant’s inequitable conduct counterclaim.

Securities class action lawsuit

On March 13 and March 19, 2015, plaintiffs Brad Christi and Roger D. Holford each filed, respectively, a lawsuit against Inogen, Raymond Huggenberger, Inogen’s President and Chief Executive Officer, and Alison Bauerlein, Inogen’s Executive Vice President and Chief Financial Officer, in the United States District Court for the Central District of California on behalf of a purported class of purchasers of our securities between November 12, 2014 and March 11, 2015. The complaints alleged that Inogen, Mr. Huggenberger and Ms. Bauerlein violated Section 10(b) of the Securities Exchange Act of 1934, as amended (the Exchange Act), and Rule 10b-5 promulgated thereunder, and that Mr. Huggenberger and Ms. Bauerlein violated Section 20(a) of the Exchange Act. Specifically, the complaints alleged that during the purported class period our financial statements and disclosures concerning internal controls over financial reporting were materially false and misleading. The complaints sought compensatory damages in an unspecified amount, costs and expenses, including attorneys’ fees and expert fees, prejudgment and post-judgment interest and such other relief as the court deemed proper. On May 7, 2015, plaintiff Roger D. Holford filed a notice of voluntary dismissal without prejudice pursuant to Federal Rule of Civil Procedure Rule 41(a)(1)(A) in the second filed action. On June 29, 2015, plaintiff Brad Christi filed a notice of voluntary dismissal without prejudice pursuant to Federal Rule of Civil Procedure Rule 41(a)(1)(A) in the first filed action. The case was closed by the Court as of June 29, 2015.

The Company is party to various legal proceedings arising in the normal course of business. The Company carries insurance, subject to deductibles under the specified policies, to protect against losses from certain types of legal claims. The Company does not anticipate that any of these proceedings will have a material impact on the Company.

6. Stock incentive plans

The Company has a 2012 Stock Incentive Plan (2012 Plan) under which the Company granted options to purchase shares of its common stock. As of June 30, 2015, options to purchase 713,776 shares of common stock remained outstanding under the 2012 Plan. The 2012 Plan was terminated in connection with the Company's initial public offering, and accordingly, no new options are available for issuance under this plan. The 2012 Plan continues to govern outstanding awards granted thereunder.

The Company has a 2002 Stock Incentive Plan (2002 Plan) as amended, under which the Company granted options to purchase shares of its common stock. As of June 30, 2015, options to purchase 548,249 shares of common stock remained outstanding under the 2002 Plan. The 2002 Plan terminated in March 2012 in connection with the adoption of the 2012 Plan, and, accordingly, no new options are available for issuance under this plan. The 2002 Plan continues to govern outstanding awards granted thereunder.

The Company's board of directors adopted and its stockholders approved a 2014 Equity Incentive Plan (2014 Plan) effective immediately prior to the effectiveness of its initial public offering. The 2014 Plan provides for the grant of incentive stock options, within the meaning of Section 422 of the Internal Revenue Code, to the Company's employees and any parent and subsidiary corporation's employees, and for the grant of nonstatutory stock options, restricted stock, restricted stock units, stock appreciation rights, performance units and performance shares to its employees, directors and consultants and its parent and subsidiary corporations' employees and consultants.

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As of June 30, 2015, a total of 1,724,487 shares of common stock have been reserved for issuance pursuant to the 2014 Plan, of which options to purchase 1,304,564 shares of the Company's common stock were outstanding, and 410,367 shares of common stock remained available for issuance. The shares to be reserved for issuance under the 2014 Plan will include shares returned to the 2002 Plan, 2012 Plan and the 2014 Plan as a result of expiration or termination of awards (provided that the maximum number of shares that may be added to the 2014 Plan pursuant to such previously granted awards under the 2002 Plan and 2012 Plan is 2,328,569 shares). The number of shares available for issuance under the 2014 Plan also includes an annual increase on the first day of each fiscal year equal to the least of:

- 895,346 shares;
- 4% of the outstanding shares of common stock as of the last day of the Company's immediately preceding fiscal year; or
- such other amount as the Company's board of directors may determine.

For 2015, an additional 762,373 shares were added to the 2014 Plan share reserve pursuant to the provision described above.

Options typically expire between seven and ten years from the date of grant and vest over one to four year terms. Options have been granted to employees, directors and consultants of the Company at the deemed fair market value, as determined by the board of directors, of the shares underlying the options at the date of grant.

The activity for stock options under the Company's stock plans is as follows:

	Options	Price per share	Weighted-average exercise price	Remaining weighted-average contractual terms (in years)	Per share average intrinsic value
Outstanding as of December 31, 2014	2,261,633	$0.60-$24.52	$ 7.31	6.43	$ 24.06
Granted	582,970	38.54	38.54		
Exercised	(268,228)	0.60-16.62	1.41		
Forfeited	(9,786)	0.75-16.62	4.46		

Expired	—	—	—		
Outstanding as of June 30, 2015	2,566,589	0.60-38.54	15.03	6.24	29.57
Vested and exercisable as of June 30, 2015	1,112,609	0.60-18.93	4.39	5.59	40.21
Vested and expected to vest as of June 30, 2015	2,438,494	$0.60-$38.54	$ 14.84	6.20	$ 29.76

The Company's board of directors adopted and its stockholders approved a 2014 Employee Stock Purchase Plan (ESPP) effective immediately prior to the effectiveness of its initial public offering. The ESPP provides for the grant to all eligible employees an option to purchase stock under the ESPP, within the meaning Section 423 of the Internal Revenue Code. The ESPP permits participants to purchase common stock through payroll deductions of up to 15% of their eligible compensation, which includes a participant's base straight time gross earnings, incentive compensation, bonuses, overtime and shift premium, but exclusive of payments for equity compensation and other similar compensation. A participant may purchase a maximum of 1,500 shares during a purchase period. Amounts deducted and accumulated by the participant are used to purchase shares of the Company's common stock at the end of each six-month period. The purchase price of the shares will be 85% of the lower of the fair market value of the Company's common stock on the first trading day of each offering period or on the exercise date. The offering periods are currently approximately six months in length beginning on the first business day on or after March 1 and September 1 of each year and ending on the first business day on or after September 1 and March 1 approximately six months later.

As of June 30, 2015, a total of 309,299 shares of common stock have been reserved for sale pursuant to the ESPP. The number of shares available for sale under the ESPP includes an annual increase on the first day of each fiscal year.

- 179,069 shares
- 1.5% of the outstanding shares of the Company's common stock on the last day of the Company's immediately preceding fiscal year; or
- such other amount as may be determined by the administrator.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

For 2015, an additional 179,069 shares were added to the ESPP share reserve pursuant to the provision described above.

The activity for the ESPP is as follows:

	First Offering Period	Second Offering Period
Employee accumulated payroll deductions	$414	$343
Total shares purchased	30,358	18,551
Payroll deductions used to purchase shares	$413	$342
Transfer to next offering period	$1	$1
FMV at enrollment date per share	$16.00	$21.69
FMV at purchase date per share	$21.69	$33.62
Purchase price per share	$13.60	$18.44

Stock-based compensation expense recognized for the three months and six months ended June 30, 2015 for the ESPP was $105 and $190, respectively, and is combined with the 2014 Plan compensation expense for a total compensation expense of $809 and $1,327 for the three months and six months ended June 30, 2015, respectively.

The number of equity awards available for grant under the 2014 Plan as of June 30, 2015 and December 31, 2014 was 410,367 and 221,178, respectively.

Employee stock-based compensation expense recognized for the six months ended June 30, 2015 and June 30, 2014 was calculated based on awards ultimately expected to vest and has been reduced for estimated forfeitures at a rate of 7.5% and 7.3%, respectively, based on the Company’s historical option cancellations. ASC 718 requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates.

For the three months ended June 30, 2015 and June 30, 2014, stock-based compensation expense recognized under ASC 718, included in cost of sales, sales and marketing expense, general and administrative expense, and research and development expense, totaled $809 and $535, respectively, and for the six months ended June 30, 2015 and June 30, 2014 was $1,327 and $666, respectively. The unrecognized compensation expense related to non-vested share based compensation granted under the Plans as of June 30, 2015 and June 30, 2014 was $11,830 and $5,438, respectively.

7. Warrants

In connection with certain of its previous convertible preferred stock issuances, convertible debt financings, and other financing arrangements, the Company had issued warrants for shares of its common stock.

A summary of outstanding common stock warrants as of June 30, 2015 is as follows:

Security	Number of warrants	Exercise price/share	Expiration date
Common stock	15,218	$ 0.30	2017-2019

8. Subsequent Events

Resignation of Director

On August 3, 2015, Timothy Petersen notified the Company that he has resigned as a member of its board of directors; the Compensation, Nominating, and Governance Committee; and the Audit Committee, effective immediately. Mr. Petersen’s resignation was not the result of any disagreement with the Company relating to the Company’s operations, policies or practices. The board of directors has reduced the size of the Compensation, Nominating, and Governance Committee by one member following the departure of Mr. Petersen.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(amounts in thousands, except share and per share amounts)

Appointment of Director

On August 3, 2015, the Board appointed R. Scott Greer to the Board, effective immediately. Mr. Greer will serve as a Class I director, with a term expiring at the annual meeting of stockholders to be held in 2015. In addition, on the same date, the board of directors appointed Mr. Greer as a member of the Audit Committee, replacing Timothy Petersen. Since June 2003, Mr. Greer has served on numerous public and private boards and has extensive corporate governance experience. Mr. Greer holds a B.A. in economics from Whitman College and an M.B.A. from Harvard University. He also was a certified public accountant.

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

The following discussion and analysis should be read together with our financial statements and the condensed notes to those statements included elsewhere in this Quarterly Report on Form 10-Q. This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, or (Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended, or (Exchange Act), that are based on our management's beliefs and assumptions and on information currently available to our management. The forward-looking statements are contained principally in the section entitled "Risk Factors" and this Management's Discussion and Analysis of Financial Condition and Results of Operations. Forward-looking statements include, but are not limited to, statements concerning the following:

- information concerning our possible or assumed future cash flow, revenue, sources of revenue and results of operations, operating and other expenses;
- our assessment of the impact from competitive bidding and the Centers for Medicare and Medicaid Services rules;
- our ability to develop new products, including our fourth-generation portable oxygen concentrator, improve our existing products and increase the value of our products;
- market share expectations, unit sales, business strategies, financing plans, expansion of our business, competitive position, industry environment, potential growth opportunities;
- our expectations regarding the market size, market growth and the growth potential for our business;
- our ability to sustain and manage growth, including our ability to develop new products and enter new markets;
- our expectations regarding the average selling price and manufacturing costs of our products;
- the effects of seasonal trends on our results of operations;
- our expectations regarding the launch and specifications of our upgraded Inogen One G3 and our fourth-generation portable oxygen concentrator; and
- the effects of competition.

Forward-looking statements include statements that are not historical facts and can be identified by terms such as "anticipates," "believes," "could," "seeks," "estimates," "expects," "intends," "may," "plans," "potential," "predicts," "projects "would," or similar expressions and the negatives of those terms.

Forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause our actual results, performance, or achievements to be materially different from any future results, performance, or achievements expressed or implied by the forward-looking statements. We discuss these risks in greater detail in Part II, Item 1A, "Risk Factors," elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K filed with the Securities and Exchange Commission, or SEC. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

Except as required by law, we assume no obligation to update these forward-looking statements, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements, even if new information becomes available in the future. You should read this Quarterly Report on Form 10-Q completely and with the understanding that our actual future results may be materially different from what we expect.

"Inogen," "Inogen One," "Inogen One G2," "Inogen One G3," "Oxygenation," "Live Life in Moments, not Minutes," "Never B Out of Oxygen," "Oxygen Therapy on Your Terms," "Oxygen.Anytime.Anywhere," "Reclaim Your Independence," "Intelligent Delivery Technology," "Inogen At Home," and the Inogen design are trademarks or registered trademarks with the United States Patent and Trademark Office of Inogen, Inc. "Inogen One G3" is a pending application with the United States Patent and Trademark Office. We own trademark registrations for the mark "Inogen" in Australia, Canada, South Korea, Mexico, and Europe (European Community registration), and we own pending applications for "Inogen"

and “ ” in Japan. We own trademark registrations for the mark “Inogen One” in Australia, Canada, China, South Korea, Mexico, and Europe (European Community registration). We own trademark registrations for the mark “Satellite Conserver” in Canada and China. We own trademark registrations for the mark “Inogen At Home” in Europe (European Community Registration). Other service marks, trademarks, and trade names referred to in this Quarterly Report on Form 10-Q are the property of their respective owners.

In this Quarterly Report on Form 10-Q, “we,” “us” and “our” refer to Inogen, Inc.

Unless otherwise specifically indicated, all amounts herein are expressed in thousands, except for share quantity, per share data, and unit counts. The following discussion of our financial condition and results of operations should be read together with our financial statements and the accompanying condensed notes to those statements included elsewhere in this document. Also, forward-looking statements represent our management's beliefs and assumptions only as of the date of this Quarterly Report on Form 10-Q.

Critical accounting policies and significant estimates

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements which have been prepared in accordance with generally accepted accounting principles in the United States, or (GAAP). The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets and liabilities and related disclosure of contingent assets and liabilities, revenue and expenses at the date of the financial statements. Generally, we base our estimates on historical experience and on various other assumptions in accordance with GAAP that we believe to be reasonable under the circumstances. Actual results may differ from these estimates and such differences could be material to the financial position and results of operations.

There have been no material changes in our critical accounting policies and estimates in the preparation of our financial statements during the three months and six months ended June 30, 2015 compared to those disclosed in our Annual Report on Form 10-K for the year ended December 31, 2014, as filed with the Securities and Exchange Commission, or (SEC) on April 27, 2015.

Overview

We are a medical technology company that primarily develops, manufactures and markets innovative portable oxygen concentrators used to deliver supplemental long-term oxygen therapy to patients suffering from chronic respiratory conditions. Traditionally, these patients have relied on stationary oxygen concentrator systems for use in the home and oxygen tanks or cylinders for mobile use. The tanks and cylinders must be delivered regularly and have a finite amount of oxygen, which limits patient mobility and requires patients to plan activities outside of their homes around delivery schedules. Additionally, patients must attach long, cumbersome tubing to their stationary concentrators simply to enable mobility within their homes. We refer to this traditional delivery approach as the delivery model. Our proprietary Inogen One systems are devices that concentrate the air around them to offer a single source of supplemental oxygen anytime, anywhere. Using our portable systems, patients can eliminate their dependence on stationary concentrators and tank and cylinder deliveries, thereby improving quality-of-life and fostering mobility.

In May 2004, we received 510(k) clearance from the U.S. Food and Drug Administration, or the FDA, for our Inogen One G1. From our launch of the Inogen One G1 in 2004, through 2008, we derived our revenue almost exclusively from sales to healthcare providers and distributors. In December 2008, we acquired Comfort Life Medical Supply, LLC in order to secure access to the Medicare rental market and began accepting Medicare reimbursement for our oxygen solutions in certain states. At the time of the acquisition, Comfort Life Medical Supply, LLC had an active Medicare billing number but few other assets and limited business activities. In January 2009, following the acquisition of Comfort Life Medical Supply, LLC, we initiated our direct-to-consumer marketing strategy and began selling Inogen One systems directly to patients and building our Medicare rental business in the United States. In April 2009, we became a Durable, Medical Equipment, Prosthetics, Orthotics, and Supplies accredited Medicare supplier by the Accreditation Commission for Health Care for our Goleta, California facility for Home/Durable Medical Equipment Services for oxygen equipment and supplies. In addition, in May 2015, we again received notice of accreditation approval from the Accreditation Commission for Health Care for all five locations we conduct business effective from May 8, 2015 through May 7, 2018. We believe we are the only portable oxygen concentrator manufacturer that employs a direct-to-consumer marketing strategy in the United States, meaning we advertise

directly to patients, process their physician paperwork, provide clinical support as needed and bill Medicare or insurance on their behalf.

We derive a majority of our revenue from the sale and rental of our Inogen One systems and related accessories to patients, insurance carriers, home healthcare providers and distributors. We sell multiple configurations of our Inogen One systems with various batteries, accessories, warranties, power cords and language settings. We also rent our products to Medicare beneficiaries and patients with other insurance coverage to support their oxygen needs as prescribed by a physician as part of a care plan. Our goal is to design, build and market oxygen solutions that redefine how oxygen therapy is delivered. To accomplish this goal and to grow our revenue, we intend to continue to:

- Expand our sales and marketing channels. We will continue to hire additional internal sales representatives to drive our direct-to-consumer marketing efforts. During the year ended December 31, 2014, we increased our internal sales representatives from 108 to 129. In 2014, we experienced headcount turnover of our internal sales team of 22.1%. Typically, we expect new sales representatives to take 4-6 months to reach full productivity. Additionally, we are building a physician referral channel that currently consists of twelve sales representatives up from eleven as of December 31, 2013.

Lastly, we are focused on building our international and domestic business-to-business partnerships, including relationships with distributors, key accounts, resellers, and private label partners.

- Invest in our product offerings to develop innovative products. We expended $1.0 million and $0.9 million for the three months ended June 30, 2015 and June 30, 2014, respectively, and $1.8 million and $1.5 million for the six months ended June 30, 2015 and June 30, 2014, respectively, in research and development expenses, and we intend to continue to make such investments in the foreseeable future. We expect to launch an upgraded Inogen One G3 product by year-end 2015 and we expect this product to have increased oxygen output and be less expensive to manufacture than our current Inogen One G3 product. We also expect to launch our fourth-generation portable oxygen concentrator, the Inogen One G4, in the first half of 2016 and we expect this product to be smaller, lighter, and less expensive to manufacture than our Inogen One G3 product.
- Secure contracts with healthcare payors and insurers. Based on our patient population, we estimate that at least 30% of oxygen therapy patients are covered by non-Medicare payors, and that these patients often represent a younger, more active patient segment. By becoming an in-network provider with more insurance companies, we can reduce the patients' co-insurance and deductible obligations on their oxygen services, which we believe will allow us to attract additional patients to our Inogen One and Inogen At Home® solutions.

We have been developing and refining the manufacturing of our Inogen One systems over the past eleven years. While nearly all of our manufacturing and assembly processes were originally outsourced, assembly of the manifold, compressor, sieve bed and concentrator is now conducted in-house in order to improve quality control and reduce cost. Additionally, we use lean manufacturing practices to maximize manufacturing efficiency. We rely on third-party manufacturers to supply several components of our Inogen One systems and Inogen At Home systems. We typically enter into supply agreements for these components that specify quantity and quality requirements and delivery terms. In certain cases, these agreements can be terminated by either party upon relatively short notice. We have elected to source certain key components from single sources of supply, including our batteries, motors, valves, and some molded plastic components. While alternative sources of supply are readily available for these components, we believe that maintaining a single-source of supply allows us to control production costs and inventory levels and to manage component quality.

Historically, we have generated a majority of our revenue from sales and rentals to customers in the United States. For both the three months and six months ended June 30, 2015 and June 30, 2014, approximately 24% and 20%, respectively, of our total revenue was from customers outside the United States, primarily in Europe. To date, most of our revenue has been denominated in United States dollars. As of June 30, 2015, we sold our products in 44 countries outside the United States through distributors or directly to large "house" accounts, which include gas companies and home oxygen providers. In those instances, we sell to and bill the distributor or "house" accounts directly, leaving responsibility for the patient billing, support and clinical setup to the local provider.

Our total revenue increased $13.6 million to $44.0 million for the three months ended June 30, 2015 from $30.4 million for the three months ended June 30, 2014 and increased $23.8 million to $77.8 million for the six months ended June 30, 2015 from $54.0 million for the six months ended June 30, 2014. Both period increases are primarily due to growth in sales revenue associated with the increases in business-to-business sales and direct-to-consumer sales of our Inogen One systems and new product launches and growth in rental revenue associated with an increase in the number of patients using Medicare or private payors to rent our products. We generated net income of $3.5 million and $2.3 million for the three months ended June 30, 2015 and June 30, 2014, respectively. We generated net income of $5.0 million and $3.2 million for the six months ended June 30, 2015 and June 30, 2014, respectively. We generated Adjusted EBITDA of $9.6 million and $7.4 million for the three months ended June 30, 2015 and June 30, 2014, respectively. We generated Adjusted EBITDA of $15.9 million and $11.8 million for the six months ended June 30, 2015 and June 30, 2014, respectively. As of June 30, 2015, our accumulated deficit was $51.7 million.

Sales revenue

Our future financial performance will be driven in part by the growth in sales of our Inogen One systems, and, to a lesser extent, sales of batteries, other accessories, and sales of our Inogen At Home stationary oxygen concentrators. We plan to grow our system sales in the coming years through multiple strategies including: expanding our direct-to-consumer sales efforts through hiring additional sales representatives, investing in consumer awareness, expanding our sales infrastructure and efforts outside of the United States, expanding our business-to-business sales through key partnerships, and enhancing our product offerings through additional product launches. As our product offerings grow, we solicit feedback from our customers and focus our research and development efforts on continuing to improve patient preference and reduce the total cost of the product, in order to further drive sales of our products.

Our direct-to-consumer sales process involves numerous interactions with the individual patient, the physician and the physician’s staff, and includes an in-depth analysis and review of our product, the patient’s diagnosis and prescribed oxygen therapy, including procuring an oxygen prescription and assessing the patient’s available insurance benefits. The patient may consider whether

to finance the product through an Inogen-approved third party or purchase the equipment. Product is not deployed until both the prescription and payment are received. Once product is deployed, the patient has 30 days to return the product, subject to the payment of a minimal processing and handling fee. Approximately 10% of consumers who purchase a system return the system during this 30-day return period.

Our business-to-business efforts are focused on selling to home medical equipment distributors, oxygen providers, resellers, and private label partners who are based inside and outside of the United States. This process involves interactions with various key customer stakeholders, including sales, purchasing, product testing, and clinical personnel. Businesses that have patient demand that can be met with our oxygen concentrator systems place purchase orders to secure product deployment. This may be influenced based on outside factors, including the result of tender offerings, changes in insurance plan coverage, and overall changes in the net oxygen therapy patient population. Products are shipped FOB Inogen domestically, and based on financial history and profile, businesses may either prepay or receive extended terms. Products are shipped both FOB (Freight on Board) Inogen dock and DDP (Delivery Duty Paid) for international shipments depending on the shipper used. DDP shipments are Inogen's property until title has changed which is upon duty being paid. As a result of these factors, product purchases can be subject to changes in demand by customers.

We sold 16,400 systems in the three months ended June 30, 2015 compared to 9,200 systems for the same period in 2014. We sold 27,400 systems for the first six months in 2015 compared to 15,500 systems for the same period in 2014. Management focuses on system sales as an indicator of current business success.

Rental revenue

Our rental process involves numerous interactions with the individual patient, the physician and the physician's staff. The process includes an in-depth analysis and review of our product, the patient's diagnosis and oxygen needs, and their medical history to confirm the appropriateness of our product for the patient's oxygen therapy and compliance with Medicare and private payor billing requirements, which often necessitates additional physician evaluation and/or testing as well as a Certificate of Medical Necessity. Once the product is deployed, the patient receives direction on product use and receives a clinical titration from our licensed staff to confirm the product meets the patient's needs prior to billing. As a result, the time from initial contact with a customer to billing can vary significantly and be up to one month or longer.

We plan to grow our rental revenue in the coming years through multiple strategies, including expanding our direct-to-consumer marketing efforts through hiring additional sales representatives and investing in patient awareness and physician-based sales, securing additional insurance contracts and continuing to enhance our product offerings through additional product launches. In addition, patients may come off of our services due to death, a change in their condition, a change in location, a change in provider or other factors. In each case, we maintain asset ownership and can redeploy assets as appropriate following such events. Given the length and uncertainty of our patient acquisition cycle and potential returns we have in the past experienced, and likely will in the future experience, there may be fluctuations in our net new patient setups on a period-to-period basis.

As the rental patient base increases, this rental model generates recurring revenue with minimal additional sales and general and administrative expenses. A portion of rentals include a capped rental period when no additional reimbursement will be allowed unless additional criteria are met. In this scenario, the ratio of billable patients to patients on service is critical to maintaining rental revenue growth as patients on service increases. Medicare has noted that a small percentage of beneficiaries, approximately 25%, based on their review of Medicare claims, reach the 36th-month and enter the capped rental period. Our capped patients as a percentage of total patients on service was approximately 14.4% as of June 30, 2015, which is similar to the capped patients as a percentage of total patients on service of approximately 14.5% as of June 30, 2014. The percentage of capped patients may fluctuate over time as

new patients come on service, patients come off of service before and during the capped rental period, and existing patients enter the capped rental period. We cannot predict the impact to rental revenues in future periods associated with capped patients on service.

As of June 30, 2015, we had 31,600 oxygen rental patients, an increase from 25,100 oxygen rental patients as of June 30, 2014. Management focuses on rental revenue as an indicator of current business success and a leading indicator of likely future rental revenue; however, actual rental revenue recognized is subject to a variety of other factors, including reimbursement levels by patient zip code, the number of capped patients, write-offs for uncollectable balances, and adjustments for patients in transition.

Reimbursement

We rely heavily on reimbursement from Medicare, and secondarily from private payors and Medicaid, for our rental revenue. For the three months and six months ended June 30, 2015, approximately 73% of our rental revenue was derived from Medicare. The U.S. list price for our stationary oxygen rentals (HCPCS E1390) is $260 per month and for our oxygen generating portable equipment (OGPE) rentals (HCPCS E1392) is $70 per month. The current standard Medicare allowable effective January 1, 2015 for stationary

oxygen rentals (E1390) is $180.92 per month and for OGPE rentals (E1392) is $51.63 per month. These are the two primary codes that we bill to Medicare and other payors for our oxygen product rentals.

As of January 1, 2011, Medicare has phased in a program called competitive bidding. Competitive bidding impacts the amount Medicare pays suppliers of durable medical equipment, including portable oxygen concentrators. The program is defined geographically, with suppliers submitting bids to provide medical equipment for a specific product category within that geography. Once bids have been placed, an individual company's bids across products within the category are aggregated and weighted by each product's market share in the category. The weighted average price is then indexed against competitors. Medicare determines a "clearing price" out of these weighted average prices at which sufficient suppliers have indicated they will support patients in the category, and this threshold is typically designed to generate theoretical supply that is twice the expected demand. Bids for each modality among the suppliers that made the cut are then arrayed to determine what Medicare will reimburse for each product category. The program has strict anti-collusion guidelines to ensure bidding is truly competitive. Competitive bidding contracts last up to three years once implemented, after which they are subject to a new round of bidding. Discounts off the standard Medicare allowable occur in competitive bidding Metropolitan Statistical Areas where contracts have been awarded as well as in cases where private payors pay less than this allowable. Current Medicare payment rates in competitive bidding areas are at 48-64% of the standard Medicare allowable for stationary oxygen rentals (average of $93.29 per month) and OGPE rentals are at 70-92% of the standard Medicare allowable (average of $42.33 per month). Competitive bidding rates are based on the zip code where the patient resides. Rental revenue includes payments for product, disposables, and customer service/support.

The following table sets forth the current Medicare standard allowable reimbursement rates and the weighted average reimbursement rates applicable in Metropolitan Statistical Areas covered by rounds one and two of competitive bidding. The round one re-compete was completed in the same Metropolitan Statistical Areas as round one for the next three year period starting January 1, 2014 when the original contracts expired.

	Medicare standard allowable effective 1/1/15	Round two weighted average 7/1/13-6/30/16	Round one re-compete weighted average 1/1/14-12/31/16
E1390	$ 180.92	$ 93.07	$ 95.74
E1392	51.63	42.72	38.08
Total	$ 232.55	$ 135.79	$ 133.82
% of standard		58 %	58 %

In addition to reducing the Medicare reimbursement rates in the Metropolitan Statistical Areas, the competitive bidding program has effectively reduced the number of oxygen suppliers that can participate in the Medicare program. We believe that more than 75% of existing oxygen suppliers were eliminated in round one of competitive bidding, which was implemented January 1, 2011 in 9 Metropolitan Statistical Areas. Round two of competitive bidding was implemented July 1, 2013 in 91 Metropolitan Statistical Areas and we believe the impact on the number of oxygen suppliers was similar to round one. We believe that 59% of the market was covered by round one and round two of competitive bidding.

Cumulatively in rounds one, two and round one re-compete, we were offered contracts for a substantial majority of the competitive bidding areas and products for which we submitted bids. However, there is no guarantee that we will garner additional market share as a result of these contracts. The contracts include products that may require us to subcontract certain services or products to third parties, which must be approved by the Centers for Medicare & Medicaid Services.

Following round one of competitive bidding, we were excluded from the Kansas City-MO-KS, Miami-Fort Lauderdale-Pompano-FL, and Orlando-Kissimmee-FL competitive bidding areas and Honolulu-Hawaii, where we have never maintained a license. After round one re-compete of competitive bidding, we gained access to Kansas City-MO-KS and were excluded from the following competitive bidding areas: Cleveland-Elyria-Mentor-OH, Cincinnati-Middletown-OH, Miami-Fort Lauderdale-Pompano-FL, Orlando-Kissimmee-FL, Pittsburg-PA, and Riverside-San Bernardino-Ontario-CA. After round two of competitive bidding, we were excluded from an additional 10 competitive bidding areas, including Akron-OH, Cape Coral-Fort Myers-FL, Deltona-Daytona Beach-Ormond Beach-FL, Jacksonville-FL, Lakeland-Winter Haven-FL, North Port-Bradenton-Sarasota-FL, Ocala, Palm Bay-Melbourne-Titusville-FL, Tampa-St. Petersburg-Clearwater-FL and Toledo-OH. Collectively, we have incrementally lost access to approximately seven percent of the Medicare market as of July 1, 2013. As a result, on a going forward basis we will continue to have access to approximately 90% of the Medicare market based on our analysis of the 92 competitive bidding areas that we have won out of the 109 competitive bidding areas, representing 59% of the market, with the remaining 41% of the market not subject to competitive bidding. The incremental loss of access to approximately seven percent of the Medicare market is not expected to have a

material adverse impact on our rental business. Medicare revenue, including patient co-insurance and deductible obligations, represented 19.3% of our total revenue in the three months ended June 30, 2015 and 21.0% of our total revenue in the six months ended June 30, 2015. We expect the decline in total revenue resulting from the loss of competitive bidding contract in the areas that we were excluded from to be partially offset by the grandfathering of existing Medicare patients and direct sales to former Medicare patients with third party insurance coverage or who pay out-of-pocket to purchase our products. Our revenue from Medicare in the 17 competitive bidding areas where we were not offered contracts was approximately $0.4 million in the three months ended June 30, 2015 and $0.1 million in the three months ended June 30, 2014 and $0.7 million in the six months ended June 30, 2015 and $0.4 million in the six months ended June 30, 2014.

Under the Medicare competitive bidding program, providers may “grandfather” existing patients on service up to the implementation date of the competitive bidding program. This means providers may retain all existing patients and continue to receive reimbursement for them so long as the new reimbursement rate is accepted and the applicable beneficiary chooses to continue to receive equipment from the provider. Providers must either keep or release all patients under this “grandfathering” arrangement in each competitive bidding area; specific individual selection of patients for retention or release is not allowed. Providers can continue to sell equipment in competitive bid areas where they were not awarded contracts to patients paying out-of-pocket or with third-party insurance coverage.

We have elected to grandfather and retain all patients in competitive bid areas where contracts were not awarded to us. In addition, we plan to continue to accept patients in competitive bidding areas where we did not receive contracts through private insurance. We will also pursue retail sales of our equipment to patients in those areas.

For rental equipment, Medicare reimbursement for oxygen equipment is limited to a maximum of 36 months within a 60 month period and the equipment is always owned by the home oxygen provider. The provider that billed Medicare for the 36th month continues to be responsible for the patient’s care for months 37 through 60, and there is generally no additional reimbursement for oxygen generating portable equipment for these later months. The Centers for Medicare & Medicaid Services does not reimburse suppliers for oxygen tubing, cannulas and supplies that may be required for the patient. The provider is required to keep the equipment provided in working order and in some cases the Centers for Medicare & Medicaid Services will reimburse for repair costs. After the five year useful life is reached, the patient may request replacement equipment and, if he or she can be re-qualified for the Medicare benefit, a new maximum 36-month rental period would begin. The supplier may not arbitrarily issue new equipment. We have analyzed the potential impact to revenue associated with patients in the capped rental period and we have concluded it is immaterial as of June 30, 2015 and prior periods, but we will continue to monitor this patient base.

Our obligations to service assigned Medicare patients over the contract rental period include supplying working equipment that meets the patient’s oxygen needs pursuant to their doctor’s prescription and certificate of medical necessity form and supplying all disposables required for the patient to operate the equipment, including cannulas, filters, replacement batteries, carts and carry bags, as needed. If the equipment malfunctions, we must repair or replace the equipment. We determine what equipment the patient receives, and we can deploy existing used assets as long as the doctor’s requirements are met. We must also procure a recertification certificate of medical necessity from the patient’s doctor to confirm the patient’s need for oxygen therapy one year after first receiving oxygen therapy and one year after each new 36-month reimbursement period begins. These contracts are cancellable by the patient at any time and by the provider at any time as long as the patient can transition to another provider.

In addition to the adoption of the competitive bidding program, reimbursable fees for oxygen rental services in non-competitive bidding areas were eligible to receive mandatory annual Consumer Price Index for all Urban Consumers, or CPI-U, updates beginning in 2010. For 2014, the CPI-U was +1.8%, but the multi-factor productivity adjustment, “adjustment”, was -0.8%, so the net result was a 1.0% increase in fee schedule payments in 2014 for items and services not included in an area subject to competitive bidding. However, the stationary oxygen equipment codes

payment amounts, as required by statute, must be adjusted on an annual basis, as necessary, to ensure budget neutrality of the new payment class for oxygen generating portable equipment. Thus, the increase in allowable payment amounts for stationary oxygen equipment codes increased 0.5% from 2013 to 2014. For 2015, the CPI-U was +2.1%, but the adjustment was -0.6%, so the net result was a 1.5% increase in fee schedule payments in 2015 for stationary oxygen equipment for items and services not included in an area subject to competitive bidding.

As of June 30, 2015, we had 72 contracts with Medicaid and private payors. These contracts qualify us an in-network provider for these payors. As a result, patients can use our systems at the same cost as other in-network oxygen therapy solutions, including those utilizing the delivery model. Based on our patient population, we believe at least 30% of all oxygen therapy patients are covered by private payors. Private payors typically provide reimbursement at 60% to 100% of Medicare allowables for in-network plans, and private payor plans can have 36-month caps similar to Medicare although they typically do not. We anticipate that private payor reimbursement levels will generally be reset in accordance with Medicare payment amounts established through competitive bidding.

We cannot predict the full extent to which reimbursement for our products will be affected by competitive bidding or by initiatives to reduce costs for private payors. We believe that we are well positioned to respond to the changing reimbursement environment because our product offerings are innovative, patient-focused and cost-effective. We have historically been able to reduce our costs through scalable manufacturing, better sourcing, continuous innovation, and reliability improvements, as well as innovations that reduce our product service costs by minimizing exchanges, such as user replaceable batteries and oxygen filtration cartridges. As a result of bringing manufacturing and assembly largely in-house and our commitment to driving efficient manufacturing processes, we have reduced our overall system cost by 40% from 2009-2014. We intend to continue to seek ways to reduce our cost of revenue through manufacturing and design improvements.

Basis of presentation

The following describes the line items set forth in our Statements of Operations.

Revenue

We classify our revenue in two main categories: sales revenue and rental revenue. There will be fluctuations in mix between business-to-business sales, direct-to-consumer sales and rentals from period to period. In addition, we expect both the average selling price and the manufacturing cost of our products to decrease following the introduction of future generations of our Inogen One systems. Inogen One system and Inogen At Home system selling prices and gross margins for our systems may fluctuate as we introduce new products, reduce our product costs, and have changes in purchase volumes. For example, the gross margin for our Inogen One G3 is higher than our Inogen One G2. Thus, to the extent our sales of our Inogen One G3 systems are higher than sales of our Inogen One G2 systems, our overall gross margins should improve and, conversely, to the extent our sales of our Inogen One G2 systems are higher than sales of our Inogen One G3 systems, our overall gross margins should decline.

Sales revenue

Our sales revenue is derived from the sale of our Inogen One systems, Inogen At Home systems, and related accessories to patients in the United States and to home healthcare providers, distributors and resellers worldwide. Sales revenue is classified into two areas: business-to-business sales and direct-to-consumer sales. For the three months ended June 30, 2015 and June 30, 2014, business-to-business sales as a percentage of sales revenue were 63.3% and 56.9%, respectively. For the six months ended June 30, 2015 and June 30, 2014, business-to-business sales as a percentage of sale revenue were 62.7% and 55.3%, respectively. Generally, our direct-to-consumer sales have higher margins than our business-to-business sales.

We also offer a lifetime warranty for direct-to-consumer sales. For a fixed price, we agree to provide a fully functional oxygen concentrator for the remaining life of the patient. Lifetime warranties are only offered to patients upon the initial sale of oxygen equipment by us, and are non-transferable. Product sales with lifetime warranties are considered to be multiple element arrangements within the scope of ASC 605-25.

There are two deliverables when a product that includes a lifetime warranty is sold. The first deliverable is the oxygen concentrator equipment which comes with a standard warranty of three years. The second deliverable is the lifetime warranty that provides for a functional oxygen concentrator for the remaining lifetime of the patient. These two deliverables qualify as separate units of accounting.

The revenue is allocated to the two deliverables on a relative selling price method. We have vendor-specific objective evidence of selling price for the equipment. To determine the selling price of the lifetime warranty, we use our best estimate of the selling price for that deliverable as the lifetime warranty is neither separately priced nor is selling price

available through third-party evidence. To calculate the selling price associated with the lifetime warranties, management considered the profit margins of the overall business, the average estimated cost of lifetime warranties and the price of extended warranties. A significant estimate used to calculate the price and expense of lifetime warranties is the life expectancy of patients. Based on clinical studies, we estimate that 60% of patients will succumb to their disease within three years. Given the approximate mortality rate of 20% per year, we estimate on average all patients will succumb to their disease within five years. We have taken into consideration that when patients decide to buy an Inogen portable oxygen concentrator with a lifetime warranty, they typically have already been on oxygen for a period of time, which can have a large impact on their life expectancy from the time our product is deployed.

After applying the relative selling price method, revenue from equipment sales is recognized when all other revenue recognition criteria for product sales are met. Lifetime warranty revenue is recognized using the straight-line method during the fourth and fifth year after the delivery of the equipment which is the estimated usage period of the contract based on the average patient life expectancy.

Freight revenue consists of fees associated with the deployment of products internationally or domestically, when expedited freight options or minimum order quantities are not met. Freight revenue is a percentage markup of freight costs.

Rental revenue

Our rental revenue is derived from the rental of our Inogen One systems and Inogen At Home systems to patients through reimbursement from Medicare, private payors and Medicaid, which typically also includes a patient responsibility component for patient co-insurance and deductibles. Generally, our product rentals have higher gross margins than our product sales.

We recognize equipment rental revenue over the non-cancelable lease term, which is one month, less estimated adjustments, per ASC 840 — Leases. We have separate contracts with each patient that are not subject to a master lease agreement with any payor. The lease term begins on the date products are shipped to patients and are recorded at amounts estimated to be received under reimbursement arrangements with third-party payors, including Medicare, private payors, and Medicaid. Due to the nature of the industry and the reimbursement environment in which we operate, certain estimates are required to record net revenue and accounts receivable at their net realizable values. Inherent in these estimates is the risk that they will have to be revised or updated as additional information becomes available. Specifically, the complexity of many third-party billing arrangements and the uncertainty of reimbursement amounts for certain services from certain payors may result in adjustments to amounts originally recorded. Such adjustments are typically identified and recorded at the point of cash application, claim denial or account review. Amounts billed but not earned due to the timing of the billing cycle are deferred and recognized in income on a straight-line basis over the monthly billing period. For example, if the first day of the billing period does not fall on the first of the month, then a portion of the monthly billing period will fall in the subsequent month and the related revenue and cost would be deferred based on the service days in the following month. Included in rental revenue are unbilled amounts for which the revenue recognition criteria had been met as of period-end but were not billed. The estimate of unbilled rental revenue accrual is based on historical trends and estimates of future collectability.

Cost of revenue

Cost of sales revenue consists primarily of costs incurred in the production process, including costs of component materials, assembly labor and overhead, warranty, provisions for slow-moving and obsolete inventory and delivery costs for items sold. We provide a three-year or lifetime warranty on Inogen One systems sold and a three-year warranty on Inogen At Home systems sold. We established a reserve for warranty repairs based on historical warranty repair costs incurred. Provisions for warranty obligations, which are included in cost of sales revenue, are provided for at the time of shipment. Cost of rental revenue consists primarily of depreciation expense and service costs for rental assets, including material, labor, freight, consumable disposables and logistics costs. We expect the average unit costs of our Inogen One systems and Inogen At Home systems to decline in future periods as a result of our ongoing efforts to develop lower-cost systems and to improve our manufacturing processes, reduce rental service costs and increase production volume and yields.

Operating expense

Research and development

Research and development expense consists primarily of personnel-related expenses, including salaries, benefits and stock-based compensation, allocated facility costs, laboratory supplies, consulting fees and related costs, and testing costs for new product launches. We have made substantial investments in research and development since our inception. Our research and development efforts have focused primarily on the tasks required to enhance our

technologies and to support development and commercialization of new and existing products. We expect to have moderate increases in research and development expense over time.

Sales and marketing

Our sales and marketing expense primarily supports our direct-to-consumer strategy. Our sales and marketing expense consists primarily of personnel-related expenses, including salaries, commissions, benefits, and stock-based compensation for employees, and allocated facilities costs. They also include expenses for media and advertising, informational kits, public relations and other promotional and marketing activities, including travel and entertainment expenses as well as customer service and clinical services. Sales and marketing expenses increased throughout 2014 primarily due to an increase in the sales force and the increasing number of rental patients and we expect a further increase in 2015 as we continue to increase sales and marketing activities.

General and administrative

General and administrative expense consists primarily of personnel-related expenses, including salaries, benefits, and stock-based compensation for employees in our compliance, finance, medical billing, human resources, information technology, business

development and general management functions, allocated facilities costs, and bad debt expense. In addition, general and administrative expense includes professional services, such as legal, patent registration and defense costs, consulting and accounting services. We expect general and administrative expenses to increase in future periods as the number of administrative personnel grows and we continue to introduce new products, broaden our customer base and grow our business. We also expect legal, accounting and compliance costs to increase due to costs associated with being a public company.

Other income (expense), net

Other income (expense), net consists primarily of interest expense related to our revolving credit and term loan agreement in the prior year and interest income driven by the interest accruing on cash, cash equivalents and short-term investments. Other income (expense) also includes the change in valuation of warrant liability based on the Monte Carlo valuation model in the prior year as well as net foreign currency translation losses in the current year.

Results of operations

Comparison of three months ended June 30, 2015 and June 30, 2014

Revenue

	Three months ended June 30,		Change 2015 vs. 2014		% of Revenue	
	2015	2014	$	%	2015	2014
Sales revenue	$32,385	$20,464	$11,921	58.3%	73.6 %	67.3 %
Rental revenue	11,644	9,929	1,715	17.3%	26.4 %	32.7 %
Total revenue	$44,029	$30,393	$13,636	44.9%	100.0%	100.0%

Sales revenue increased $11.9 million to $32.4 million for the three months ended June 30, 2015 from $20.5 million for the three months ended June 30, 2014, or an increase of 58.3% over the comparable year. The increase was primarily attributable to an increase in the number of systems sold as the adoption of portable oxygen concentrators improved. In addition, the increase in the number of systems sold resulted from an increase in direct-to-consumer sales in the United States due to increased sales and marketing efforts and an increase in business-to-business sales worldwide and within the domestic United States.

Rental revenue increased $1.7 million to $11.6 million for the three months ended June 30, 2015 from $9.9 million for the three months ended June 30, 2014, or an increase of 17.3% over the comparable year. The increase was primarily attributable to the increase in net rental patients to 31,600 as of June 30, 2015 from 25,100 as of June 30, 2014, additional marketing efforts, increased sales personnel and productivity improvements. The increase in rental revenue was partially offset by higher rental revenue adjustments as a percentage of total rental revenue in the three months ended June 30, 2015 versus the three months ended June 30, 2014.

A recent ruling from the Centers for Medicare & Medicaid Services (CMS) has outlined the expansion of Competitive Bidding to certain previously unbid areas by applying regional pricing averages to unbid areas with 110% of regional prices to be paid for defined rural and frontier areas. While we are monitoring the implementation of this ruling, we

believe that the net effect of the ruling would be an approximately 2.5-3.5% decrease in 2016 total revenue since this pricing will be applied partially from January 1, 2016 to June 30, 2016 and completely starting on July 1, 2016. Medicare is 21.0% of our total revenue in the six months ended June 30, 2015, and we estimate that 41% of the Medicare markets will be subject to this reimbursement reduction. We also estimate that on average the rates will be reduced by 35-40% in these areas. CMS has also re-bid the Round Two Re-Compete schedule beginning in the first quarter of 2015 for contracts set to expire June 30, 2016. CMS has announced the Round One Re-Compete plan to re-bid for contracts set to expire December 31, 2016. For additional discussion of the impact of the recent competitive bidding proposals, please see "— Risk Factors" herein.

	Three months ended