Inogen Inc
Form 10-Q
November 03, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended September 30, 2016

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 No

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 No

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

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

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

As of October 31, 2016, the registrant had 20,260,695 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)

	September 30, 2016	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	$ 86,009	$ 66,106
Marketable securities	22,331	16,793
Accounts receivable, net	29,717	19,872
Inventories, net	16,499	8,648
Deferred cost of revenue	439	397
Income tax receivable	1,612	2,158
Prepaid expenses and other current assets	1,470	870
Total current assets	158,077	114,844
Property and equipment		
Rental equipment, net	54,684	54,677
Manufacturing equipment and tooling	5,850	4,680
Computer equipment and software	4,663	4,503
Furniture and equipment	757	732
Leasehold improvements	811	978
Land and building	125	125
Construction in process	430	578
Total property and equipment	67,320	66,273
Less accumulated depreciation	(40,485)	(35,593)
Property and equipment, net	26,835	30,680
Intangible assets, net	268	229
Deferred tax asset - noncurrent	9,514	15,464
Other assets	97	97
Total assets	$ 194,791	$ 161,314

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Balance Sheets (continued)

(unaudited)

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

	September 30, 2016	December 31, 2015
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable and accrued expenses	$ 20,710	$ 12,867
Accrued payroll	5,844	5,271
Current portion of long-term debt	80	315
Warranty reserve - current	1,559	1,226
Deferred revenue - current	2,035	2,323
Income tax payable	—	11
Total current liabilities	30,228	22,013
Long-term liabilities		
Warranty reserve - noncurrent	1,838	747
Deferred revenue - noncurrent	6,343	4,199
Other noncurrent liabilities	300	337
Total liabilities	38,709	27,296
Commitments and contingencies (Note 9)		
Stockholders' equity		
Common stock, $0.001 par value per share; 200,000,000 authorized; 20,244,243 and 19,782,403 shares issued and outstanding as of September 30, 2016 and December 31, 2015, respectively	20	20
Additional paid-in capital	190,202	179,143
Accumulated deficit	(34,146)	(45,108)
Accumulated other comprehensive income (loss)	6	(37)
Total stockholders' equity	156,082	134,018
Total liabilities and stockholders' equity	$ 194,791	$ 161,314

See accompanying condensed notes to the financial statements.

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Inogen, Inc.

Statements of Comprehensive Income

(unaudited)

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

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Revenue				
Sales revenue	$47,177	$29,248	$125,566	$84,682
Rental revenue	7,245	11,530	26,412	33,877
Total revenue	54,422	40,778	151,978	118,559
Cost of revenue				
Cost of sales revenue	24,271	16,046	63,824	46,501
Cost of rental revenue, including depreciation of $2,878 and $3,029 for the three months ended and $8,733 and $8,929 for the nine months ended, respectively	5,023	5,357	15,532	15,838
Total cost of revenue	29,294	21,403	79,356	62,339
Gross profit				
Gross profit-sales revenue	22,906	13,202	61,742	38,181
Gross profit-rental revenue	2,222	6,173	10,880	18,039
Total gross profit	25,128	19,375	72,622	56,220
Operating expense				
Research and development	1,350	1,116	3,897	2,954
Sales and marketing	9,679	8,132	28,220	22,623
General and administrative	8,702	6,413	23,812	19,066
Total operating expense	19,731	15,661	55,929	44,643
Income from operations	5,397	3,714	16,693	11,577
Other income (expense)				
Interest expense	(1)	(5)	(6)	(18)
Interest income	61	28	126	66
Other income (expense)	(8)	(59)	78	(215)
Total other income (expense), net	52	(36)	198	(167)
Income before provision for income taxes	5,449	3,678	16,891	11,410
Provision for income taxes	1,994	982	5,929	3,683
Net income	3,455	2,696	10,962	7,727
Other comprehensive income, net of tax				
Unrealized gain (loss) on foreign currency hedging during the period	10	—	(24)	—
	2	—	51	—

Add: reclassification adjustment for losses included in net income				
Total unrealized gain on foreign currency hedging	12	—	27	—
Unrealized gain (loss) on available-for-sale investments during the period	(4)	—	16	—
Total other comprehensive income, net of tax	8	—	43	—
Comprehensive income	$3,463	$2,696	$11,005	$7,727
Basic net income per share attributable to common stockholders (Note 5)	$0.17	$0.14	$0.55	$0.40
Diluted net income per share attributable to common stockholders (Note 5)	$0.16	$0.13	$0.52	$0.37
Weighted-average number of shares used in calculating net income per share attributable to common stockholders:				
Basic common shares	20,157,688	19,428,653	19,986,544	19,303,057
Diluted common shares	21,100,725	20,783,550	20,924,022	20,690,499

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statement of Stockholders' Equity

(unaudited)

(amounts in thousands, except share amounts)

	Common stock Shares	Amount	Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive income (loss)	Total stockholders' equity
Balance, December 31, 2014	19,059,364	$ 19	$ 174,824	$ (56,693)	$ —	$ 118,150
Stock-based compensation	—	—	2,343	—	—	2,343
Employee stock purchases	31,106	—	701	—	—	701
Stock options exercised	496,203	—	1,001	—	—	1,001
Net income	—	—	—	7,727	—	7,727
Balance, September 30, 2015	19,586,673	$ 19	$ 178,869	$ (48,966)	$ —	$ 129,922
Balance, December 31, 2015	19,782,403	20	179,143	(45,108)	(37)	134,018
Stock-based compensation	—	—	5,404	—	—	5,404
Employee stock purchases	37,378	—	1,055	—	—	1,055
Stock options exercised	424,462	—	4,600	—	—	4,600
Net income	—	—	—	10,962	—	10,962
Other comprehensive income	—	—	—	—	43	43
Balance, September 30, 2016	20,244,243	$ 20	$ 190,202	$ (34,146)	$ 6	$ 156,082

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows

(unaudited)

(amounts in thousands)

	Nine months ended September 30, 2016	2015
Cash flows from operating activities		
Net income	$10,962	$7,727
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	10,290	10,468
Loss on rental units and other fixed assets	891	889
Gain on sale of former assets	(224)	—
Provision for sales returns and doubtful accounts	8,177	5,346
Provision for rental revenue adjustments	7,783	6,364
Provision for inventory obsolescence and other inventory losses, net of recoveries	141	131
Stock-based compensation expense	5,404	2,343
Deferred tax assets	5,950	3,682
Changes in operating assets and liabilities:		
Accounts receivable	(25,812)	(13,251)
Inventories	(9,220)	(3,167)
Deferred cost of revenue	(42)	41
Income tax receivable	546	(32)
Prepaid expenses and other current assets	(600)	(774)
Accounts payable and accrued expenses	7,801	3,030
Accrued payroll	573	573
Warranty reserve	1,424	673
Deferred revenue	1,856	1,615
Income tax payable	(11)	—
Other noncurrent liabilities	(37)	(54)
Net cash provided by operating activities	25,852	25,604
Cash flows from investing activities		
Purchases of available-for-sale investments	(26,321)	(33,557)
Maturities of available-for-sale investments	20,799	14,529
Investment in intangible assets	(112)	(21)
Investment in property and equipment	(6,071)	(9,780)
Proceeds from sale of former assets	328	—
Net cash used in investing activities	(11,377)	(28,829)

(continued on next page)

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows (continued)

(unaudited)

(amounts in thousands)

	Nine months ended September 30,	
	2016	2015
Cash flows from financing activities		
Proceeds from stock options exercised	4,600	1,001
Proceeds from employee stock purchases	1,055	701
Repayment of debt from investment in intangible assets	(235)	(223)
Net cash provided by financing activities	5,420	1,479
Effect of exchange rates on cash	8	—
Net increase (decrease) in cash and cash equivalents	19,903	(1,746)
Cash and cash equivalents, beginning of period	66,106	56,836
Cash and cash equivalents, end of period	$86,009	$55,090
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	$9	$21
Cash paid (received) during the period for income taxes, net	(533)	32

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. Business overview

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 2.8, 4.8 or 7.0 pounds with a single battery. The Company’s Inogen One G4®, Inogen One G3® and Inogen One G2® have up to 2.5, 5 and 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.

Portable oxygen concentrators represented the fastest-growing segment of the Medicare oxygen therapy market between 2012 and 2015. The Company estimates based on 2015 Medicare data that patients using portable oxygen concentrators represent approximately 8% of the total addressable oxygen market in the United States, although the Medicare data does not account for cash-pay sales into the market. Based on 2015 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 oxygen concentrators to more than 196,000 patients as of September 30, 2016.

2. Basis of presentation and summary of significant accounting policies

The accompanying financial statements are unaudited. The balance sheet at December 31, 2015 has been derived from the audited financial statements of the Company. The accompanying financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (U.S. GAAP) for interim financial information, and in management’s opinion, includes all adjustments, consisting of only normal recurring adjustments, necessary for the fair statement of the Company’s financial position, its results of operations, stockholders’ equity and cash flows for the interim periods presented. The results of operations for the three and nine months ended September 30, 2016 are not necessarily indicative of the results to be expected for the full fiscal year or any other period.

The accompanying financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company’s Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on March 14, 2016. There have been no significant changes in the Company’s accounting policies from those disclosed in its Annual Report on Form 10-K filed with the SEC on March 14, 2016.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Use of estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. 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 revenue recognition, inventory and rental asset valuations and write-downs, accounts receivable allowances 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 from these estimates.

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 Statement of Cash Flows and did not change total operating, financing or investing activities as previously reported.

Recent accounting pronouncements

Income taxes pronouncements:

In November 2015, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2015-17, Balance Sheet Classification of Deferred Taxes, which simplifies the presentation of deferred income taxes. This ASU requires that deferred tax assets and liabilities be classified as noncurrent in a statement of financial position. The Company early adopted ASU No. 2015-17 effective December 31, 2015 on a prospective basis. Adoption of this ASU resulted in a reclassification of the Company's net current deferred tax asset to the net noncurrent deferred tax asset in the Company's balance sheet as of December 31, 2015. No prior periods were retrospectively adjusted.

Revenue recognition pronouncements:

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU No. 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 for those goods or services. ASU No. 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 U.S. GAAP.

In August 2015, the FASB decided to delay the effective date of ASU No. 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 the Company in the first quarter of 2018, with the option to adopt it in the first quarter of 2017. The Company is currently evaluating the impact of the Company's pending adoption of ASU No. 2014-09 on the Company's financial statements and has not yet determined the method by which the Company will adopt the standard.

In March 2016, the FASB issued ASU No. 2016-08, Revenue with Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus net), which is an amendment to ASU No. 2014-09 that improved the operability and understandability of implementation guidance versus agent considerations by clarifying the determination of principal versus agent. The implementation guidelines follow ASU No. 2014-09.

In April 2016, the FASB issued ASU No. 2016-10, Revenue with Contracts with Customers: Identifying Performance Obligations and Licensing, which is an amendment to ASU No. 2014-09 that clarifies the aspects of identifying performance obligations and the licensing implementing guidance, while retaining the related principles within those areas. The implementation guidelines follow ASU No. 2014-09.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

In May 2016, the FASB issued ASU No. 2016-12, Revenue with Contracts with Customers: Narrow-scope Improvements and Practical Expedients, which is an amendment to ASU No. 2014-09 that clarifies the objective of the collectability criterion, to allow entities to exclude amounts collected from customers from all sales taxes from the transaction price, to specify the measurement date for noncash consideration is contract inception, variable consideration guidance applies only to variability resulting from reasons other than the form of the consideration, and clarification on contract modifications at transition. The implementation guidelines follow ASU No. 2014-09.

Inventory pronouncements:

In July 2015, the FASB issued ASU No. 2015-11, Simplifying the Measurement of Inventory. The ASU requires entities to measure most inventory "at the lower of cost and net realizable value" thereby simplifying the current guidance under which an entity must measure inventory at the lower of cost or market. The ASU is effective prospectively for annual periods beginning after December 15, 2016, and interim periods within annual periods. Early application is permitted and should be applied prospectively. The adoption of ASU No. 2015-11 is not expected to have a material effect on the Company's financial statements.

Leases pronouncements:

On February 25, 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842). The new guidance will require organizations that lease assets—referred to as "lessees"—to recognize on the balance sheet the assets and liabilities for the rights and obligations created by those leases with lease terms of more than 12 months. This will increase the reported assets and liabilities – in some cases very significantly. ASU No. 2016-02 will take effect for public companies for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018. Early adoption will be permitted for all entities. The Company is currently evaluating the effect of the new lease recognition guidance and has not yet determined the impact on the Company's results of operations and financial condition.

Stock compensation pronouncements:

In March 2016, the FASB issued ASU No. 2016-09, Compensation – Stock Compensation, which simplifies the accounting for share-based payment transactions, including the income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. The ASU is effective for annual periods beginning after December 15, 2016, and interim periods within those annual periods. Certain amendments related to ASU No. 2016-09 are implemented with changes recognized on a modified retrospective transition method, retrospectively as well as prospectively. Early application is permitted for any entity in any interim or annual period. If early adoption is elected during an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. If early adoption is elected, all of the amendments must be adopted in the same period. The adoption of ASU No. 2016-09 and its impact to the financial statements is still being reviewed by the Company, and early adoption has not yet been determined.

Financial instruments pronouncements:

In June 2016, the FASB issued ASU No. 2016-13, Accounting for Credit Losses (Topic 326). The new standard requires the use of an “expected loss” model on certain types of financial instruments. The standard also amends the impairment model for available-for-sale debt securities and requires estimated credit losses to be recorded as allowances instead of reductions to amortized cost of the securities. The ASU is effective for fiscal years beginning after December 15, 2019, and interim periods within those years, with early adoption permitted. The Company is evaluating the new guidance but does not expect it to have a significant impact on the Company’s financial statement presentation or results.

Statement of cash flows pronouncements:

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230). The standard is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. The ASU is effective for fiscal years beginning after December 15, 2017, and interim periods within those years, with early adoption permitted. The Company is evaluating the new guidance but does not expect it to have a significant impact on the Company’s financial statement presentation or results.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Business segments

The Company operates and reports in only one operating and reportable segment – development, manufacturing, marketing, sales, and rental of respiratory products.

3. Fair value of financial instruments

The Company's financial instruments consist of cash and cash equivalents, marketable securities, accounts receivable, accounts payable and accrued expenses, debt and warrants. The carrying values of cash and cash equivalents, marketable securities, 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.

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 U.S. 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 is to estimate the price at which an orderly transaction to sell an asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. 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 investments, 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 investments within Level 2 of the fair value hierarchy.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

The following table summarizes fair value measurements by level for the assets measured at fair value on a recurring basis for cash, cash equivalents and marketable securities:

	As of September 30, 2016				
	Adjusted cost	Gross unrealized losses	Fair value	Cash and cash equivalents	Marketable securities
Cash	$43,454	$ —	$43,454	$ 43,454	$ —
Level 1:					
Money market accounts	39,793	—	39,793	39,793	—
Level 2:					
Certificates of deposit	14,782	—	14,782	2,762	12,020
Corporate bonds	10,321	(10)	10,311	—	10,311
Total	$108,350	$ (10)	$108,340	$ 86,009	$ 22,331

	As of December 31, 2015				
	Adjusted cost	Gross unrealized losses	Fair value	Cash and cash equivalents	Marketable securities
Cash	$52,164	$ —	$52,164	$ 52,164	$ —
Level 1:					
Money market accounts	6,725	—	6,725	6,725	—
Level 2:					
Certificates of deposit	24,047	(37)	24,010	7,217	16,793
Total	$82,936	$ (37)	$82,899	$ 66,106	$ 16,793

The following table summarizes the estimated fair value of the Company's investments in marketable securities, accounted for as available-for-sale securities and classified by the contractual maturity date of the securities:

	September 30, 2016

Due within one year	$ 15,081
Due in one year through five years	7,250
Total	$ 22,331

Derivative instruments and hedging activities

The Company transacts business in foreign currencies and has international sales and expenses denominated in foreign currencies, subjecting the Company to foreign currency risk. The Company has entered into foreign currency forward contracts, generally with maturities of twelve months or less, to reduce the volatility of cash flows primarily related to forecasted revenue denominated in certain foreign currencies. These contracts allow the Company to sell Euros in exchange for U.S. dollars at specified contract rates. Forward contracts are used to hedge forecasted sales over specific months. Changes in the fair value of these forward contracts designed as cash flow hedges are recorded as a component of accumulated other comprehensive income (loss) within stockholders' equity and are recognized in the statements of comprehensive income during the period which approximates the time the corresponding sales occur. The Company may also enter into foreign exchange contracts that are not designated as hedging instruments for financial accounting purposes. These contracts are generally entered into to offset the gains and losses on certain asset and liability balances until the expected time of repayment. Accordingly, any gains or losses resulting from changes in the fair value of the non-designated contracts are reported in other income (expense), net in the statements of comprehensive income. The gains and losses on these contracts generally offset the gains and losses associated with the underlying foreign currency-denominated balances, which are also reported in other income (expense), net.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

The Company records the assets or liabilities associated with derivative instruments and hedging activities at fair value based on Level 2 inputs in other current assets or other current liabilities, respectively, in the balance sheet. The Company had a receivable of $6 as of September 30, 2016 and a payable of $24 as of December 31, 2015. The Company classifies the foreign currency derivative instruments within Level 2 in the fair value hierarchy as the valuation inputs are based on quoted prices and market observable data of similar instruments. The accounting for gains and losses resulting from changes in fair value depends on the use of the derivative and whether it is designated and qualifies for hedge accounting.

The Company documents the hedging relationship and its risk management objective and strategy for undertaking the hedge, the hedging instrument, the hedged transaction, the nature of the risk being hedged, how the hedging instrument's effectiveness in offsetting the hedged risk will be assessed prospectively and retrospectively, and a description of the method used to measure ineffectiveness. The Company assesses hedge effectiveness and ineffectiveness at a minimum quarterly but may assess it monthly. For derivative instruments that are designed and qualify as part of a cash flow hedging relationship, the effective portion of the gain or loss on the derivative is reported in other comprehensive income (loss) and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. Gains and losses on the derivative representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current period earnings.

The Company will discontinue hedge accounting prospectively when it determines that the derivative is no longer effective in offsetting cash flows attributable to the hedge risk. The cash flow hedge is de-designated because a forecasted transaction is not probable of occurring, or management determines to remove the designation of the cash flow hedge. In all situations in which hedge accounting is discontinued and the derivative remains outstanding, the Company continues to carry the derivative at its fair value on the balance sheet and recognizes any subsequent changes in the fair value in earnings. When it is probable that a forecasted transaction will not occur, the Company will discontinue hedge accounting and recognize immediately in earnings gains and losses that were accumulated in other comprehensive income related to the hedging relationship.

Accumulated other comprehensive income (loss)

The components of accumulated other comprehensive income (loss), net of tax, were as follows:

	Unrealized gains (losses) on available-for-sale investments	Unrealized gains (losses) on cash flow hedges	Accumulated other comprehensive income (loss)
Balance as of December 31, 2015	$ (23)	$ (14)	$ (37)

Other comprehensive gain, net of tax	16	27	43
Balance as of September 30, 2016	$ (7)	$ 13	$ 6

Comprehensive income (loss) is the total net earnings and all other non-owner changes in equity. Except for net income and unrealized gains and losses on cash flow hedges and available-for-sale investments, the Company does not have any transactions or other economic events that qualify as comprehensive income (loss).

4. Balance sheet components

Cash, cash equivalents, and marketable securities

The Company considers all short-term highly liquid investments with a maturity of three months or less to be cash equivalents. Cash equivalents are recorded at cost plus accrued interest (adjusted cost), which approximates fair value which includes the unrealized gains (losses). Certificates of deposit are included in cash equivalents and marketable securities based on the maturity date of the security. Short-term investments are included in marketable securities in the current period presentation.

The Company considers investments with maturities greater than three months to be marketable securities. 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 (loss). All income generated and realized gains or losses from investments are recorded to other income (expense), net.

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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 other income (expense), net. During the three and nine months ended September 30, 2016 and 2015, respectively, no losses were recognized for other-than-temporary impairments. Cash, cash equivalents and marketable securities consist of the following:

Cash and cash equivalents	September 30, 2016	December 31, 2015
Cash	$ 43,454	$ 52,164
Money market accounts	39,793	6,725
Certificates of deposit	2,762	7,217
Total cash and cash equivalents	$ 86,009	$ 66,106
Marketable securities		
Certificates of deposit	$ 12,020	$ 16,793
Corporate bonds	10,311	—
Total marketable securities	$ 22,331	$ 16,793

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 for doubtful accounts 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 in which they become known. This 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.

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

The Company also records an allowance for rental revenue adjustments, which is recorded as a reduction of rental revenue and net rental accounts receivable balances. These adjustments result from contractual adjustments, including 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 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 rental reserve adjustments, the rental revenue adjustments account (contra rental revenue account) is charged.

As of September 30, 2016 and December 31, 2015, included in accounts receivable on the balance sheets were earned but unbilled receivables of $5,272 and $5,155, respectively. These balances reflect gross unbilled receivables prior to any allowances for adjustments and write-offs. The Company consistently applies its allowance estimation methodology from period-to-period. The Company's best estimate is made on an accrual basis and adjusted in future periods as required. Any adjustments to the prior period estimates are included in the current period. As additional information becomes known, the Company adjusts its assumptions accordingly to change its estimate of the allowance.

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

Gross accounts receivable balance concentrations by major category as of September 30, 2016 and December 31, 2015 were as follows:

Gross accounts receivable	September 30, 2016	December 31, 2015
Medicare	$ 11,204	$ 10,510
Medicaid/other government	555	683
Private insurance	3,312	4,852
Patient responsibility	2,856	3,603
Business-to-business & other receivables	18,698	6,369
Total gross accounts receivable	$ 36,625	$ 26,017

Net accounts receivable (gross accounts receivable net of allowances) balance concentrations by major category as of September 30, 2016 and December 31, 2015 were as follows:

Net accounts receivable	September 30, 2016	December 31, 2015
Medicare	$ 6,668	$ 7,441
Medicaid/other government	394	550
Private insurance	2,738	3,895
Patient responsibility	1,907	2,060
Business-to-business & other receivables	18,010	5,926
Total net accounts receivable	$ 29,717	$ 19,872

The following tables set forth the accounts receivable allowances as of September 30, 2016 and December 31, 2015:

Allowances - accounts receivable	September 30, 2016	December 31, 2015
Doubtful accounts	$ 1,192	$ 1,664
Rental revenue adjustments	5,137	4,115
Sales returns	579	366
Total allowances - accounts receivable	$ 6,908	$ 6,145

Concentration of credit risk

Financial instruments that potentially subject the Company to concentration of credit risk consist principally of cash, cash equivalents, marketable securities 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. The Company has entered into hedging relationships with a single counterparty to offset a portion of the forecasted Euro based revenues. The credit risk has been reduced due to a net settlement arrangement whereby the Company is allowed to net settle transactions with a single net amount payable by one party to the other.

Concentration of customers and vendors

The Company primarily sells its products to traditional home medical equipment providers, distributors, and resellers in the United States and in foreign countries on a credit basis. The Company primarily sells its products to consumers on a prepayment basis. No single customer represented more than 10% of the Company’s total revenue for the nine months ended September 30, 2016 and September 30, 2015. One customer represented more than 10% of the Company’s total net accounts receivable balance as of September 30, 2016, and no single customer represented more than 10% of the Company’s total net accounts receivable balance as of December 31, 2015.

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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 71.0% and 75.9% of rental revenue for the three months ended September 30, 2016 and September 30, 2015, respectively, and based on total revenue was 9.5% and 21.5% for the three months ended September 30, 2016 and September 30, 2015, respectively. Medicare's service reimbursement programs accounted for 71.6% and 74.0% of rental revenue for the nine months ended September 30, 2016 and September 30, 2015, respectively, and based on total revenue was 12.4% and 21.1% for the nine months ended September 30, 2016 and September 30, 2015, respectively. One customer represented more than 10% of the Company's total revenue for the three months ended September 30, 2016. Accounts receivable balances relating to Medicare's service reimbursement programs (including held and unbilled, net of allowances) amounted to $6,668 or 22.4% of total net accounts receivable as of September 30, 2016 as compared to $7,441, or 37.4% of total net accounts receivable as of December 31, 2015.

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 nine months ended September 30, 2016, the Company's three major vendors accounted for 22.0%, 14.9%, and 7.9%, respectively, of total raw material purchases. For the nine months ended September 30, 2015, the Company's three major vendors accounted for 23.0%, 17.4% and 8.9%, respectively, of total raw material purchases.

A portion of revenue is earned from sales outside the United States. Approximately 72.8% and 87.5% of the non-U.S. revenue for the three months ended September 30, 2016 and September 30, 2015, respectively, were invoiced in Euros. Approximately 70.7% and 74.6% of the non-U.S. revenue for the nine months ended September 30, 2016 and September 30, 2015, respectively, were invoiced in Euros. A breakdown of the Company's revenue from U.S. and non-U.S. sources for the three months and nine months ended September 30, 2016 and September 30, 2015 is as follows:

	Three months ended		Nine months ended	
	September 30,		September 30,	
	2016	2015	2016	2015
U.S. revenue	$39,470	$32,907	$113,963	$91,719
Non-U.S. revenue	14,952	7,871	38,015	26,840
Total revenue	$54,422	$40,778	$151,978	$118,559

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:

	September 30, 2016	December 31, 2015
Raw materials and work-in-progress	$ 14,497	$ 7,097
Finished goods	2,162	1,679
Less: reserves	(160)	(128)
Inventories	$ 16,499	$ 8,648

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

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	2-5 years
Computer equipment and software	2-3 years
Furniture and equipment	3-5 years
Leasehold improvements	Lesser of estimated useful life or remaining lease term

Expenditures for additions, improvements and replacements are capitalized and depreciated to a salvage value of $0. Repair and maintenance costs on rental equipment are included in cost of rental revenue on the statements of comprehensive income. Repair and maintenance expense, which includes labor, parts and freight, for rental equipment was $497 and $686 for the three months ended September 30, 2016 and September 30, 2015, respectively, and $1,930 and $1,897 for the nine months ended September 30, 2016 and September 30, 2015, respectively.

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

Depreciation and amortization expense related to property and equipment and rental equipment are summarized below for the three and nine months ended September 30, 2016 and September 30, 2015, respectively.

	Three months ended September 30,		Nine months ended September 30,	
	2016	2015	2016	2015
Rental equipment	$2,878	$3,029	$8,733	$8,929
Other property and equipment	510	510	1,484	1,475
Total depreciation and amortization	$3,388	$3,539	$10,217	$10,404

Property and equipment and rental equipment with associated accumulated depreciation is summarized below for September 30, 2016 and December 31, 2015, respectively.

Property and equipment	September 30, 2016	December 31, 2015
Rental equipment, net of allowances of $600 and $850, respectively	$ 54,684	$ 54,677
Other property and equipment	12,636	11,596
Property and equipment	67,320	66,273
Accumulated depreciation		
Rental equipment	32,731	28,894
Other property and equipment	7,754	6,699
Accumulated depreciation	40,485	35,593