Inogen Inc
Form 10-Q
November 12, 2014

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 September 30, 2014

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 (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 o No x

The total number of shares of common stock outstanding as of October 31, 2014 was 18,628,900.

TABLE OF CONTENTS

INOGEN, INC.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

Inogen, Inc.

Balance Sheets

(unaudited)

(amounts in thousands)

	September 30, 2014	December 31, 2013
Assets		
Current assets		
Cash and cash equivalents	$ 56,160	$ 13,521
Accounts receivable, net of allowances of $3,981 and $3,390 at September 30, 2014 and December 31, 2013, respectively	18,061	10,231
Inventories, net of allowances of $183 and $100 at September 30, 2014 and December 31, 2013, respectively	7,331	4,248
Deferred cost of rental revenue	423	289
Income tax receivable	-	87
Deferred tax asset - current	6,360	3,923
Prepaid expenses and other current assets	980	531
Total current assets	89,315	32,830
Property and equipment		
Rental equipment, net of allowances of $682 and $157 at September 30, 2014 and December 31, 2013, respectively	45,532	37,573
Manufacturing equipment and tooling	2,745	2,551
Computer equipment and software	3,611	2,973
Furniture and equipment	608	601
Leasehold improvements	889	887
Land and building	126	-
Construction in process	1,186	1,093
Total property and equipment	54,697	45,678
Less accumulated depreciation	(23,640)	(15,956)
Property and equipment, net	31,057	29,722
Intangible assets, net	274	215
Deferred tax asset - noncurrent	16,427	17,865

Other assets	80	1,765
Total assets	$ 137,153	$ 82,397

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, 2014	December 31, 2013
Liabilities, redeemable convertible preferred stock and stockholders' equity (deficit)		
Current liabilities		
Accounts payable and accrued expenses	$ 11,201	$ 9,219
Accrued payroll	3,732	2,898
Current portion of long-term debt	267	5,258
Warranty reserve	669	420
Deferred revenue	1,959	1,487
Income tax payable	2,647	-
Total current liabilities	20,475	19,282
Long-term liabilities		
Warranty reserve - noncurrent	503	389
Preferred stock warrant liability	-	260
Deferred revenue-noncurrent	1,878	776
Long-term debt, net of current portion	391	5,391
Total liabilities	23,247	26,098
Commitments and contingencies (Note 5)		
Redeemable convertible preferred stock		
Preferred stock, $0.001 par value per share; 10,000,000 authorized as of December 31, 2013; 0 and 9,541,631 shares issued and outstanding; liquidation preference of $0 and $136,660 at September 30, 2014 and December 31, 2013, respectively (Note 7)	-	118,671
Stockholders' equity (deficit)		
Preferred stock, $0.001 par value per share; 10,000,000 and 100,000 shares authorized; 0 and 66,666 shares issued and outstanding; liquidation preference of $0 and $250 at September 30, 2014 and December 31, 2013, respectively. (Note 7)	-	247
Common stock, $0.001 par value per share; 200,000,000 and 60,000,000 shares authorized; 18,436,802 and 280,974 shares issued and outstanding at September 30, 2014 and December 31, 2013, respectively.	18	1
Additional paid-in-capital	172,100	-
Accumulated deficit	(58,212)	(62,620)
Total stockholders' equity (deficit)	113,906	(62,372)
Total liabilities, redeemable convertible preferred stock and stockholders' equity (deficit)	$ 137,153	$ 82,397

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 September 30,		Nine months ended September 30,	
	2014	2013	2014	2013
Revenue				
Sales revenue	$ 19,425	$ 12,134	$ 54,746	$ 33,780
Rental revenue	9,968	7,643	28,673	21,901
Total revenue	29,393	19,777	83,419	55,681
Cost of revenue				
Cost of sales revenue	10,146	6,751	28,369	18,406
Cost of rental revenue, including depreciation of $2,752 and $1,955 for the three months ended and $7,512 and $4,921 for the nine months ended, respectively	4,598	3,384	13,349	8,459
Total cost of revenue	14,744	10,135	41,718	26,865
Gross profit	14,649	9,642	41,701	28,816
Operating expenses				
Research and development	798	674	2,312	1,817
Sales and marketing	5,587	4,550	17,656	13,292
General and administrative	4,697	3,532	12,654	9,796
Total operating expenses	11,082	8,756	32,622	24,905
Income from operations	3,567	886	9,079	3,911
Other income (expense)				
Interest expense	(104)	(113)	(440)	(312)
Interest income	10	3	28	9
Change in fair value of preferred stock warrant liability	-	41	36	(202)
Other income	1	-	12	209
Total other expense, net	(93)	(69)	(364)	(296)
Income before provision for income taxes	3,474	817	8,715	3,615
Provision for income taxes	1,341	43	3,408	151
Net income	$ 2,133	$ 774	$ 5,307	$ 3,464
Less deemed dividend on redeemable convertible preferred stock	-	(1,851)	(987)	(5,359)
Net income (loss)	$ 2,133	$ (1,077)	$ 4,320	$ (1,895)
Basic net income (loss) per share attributable to common stockholders (note 2)	$ 0.12	$ (3.90)	$ 0.24	$ (6.91)
Diluted net income (loss) per share attributable to common stockholders (note 2)	$ 0.11	$ (3.90)	$ 0.22	$ (6.91)

Weighted-average number of shares used in calculating income (loss) per share attributable to common stockholders (note 2):				
Basic common shares	18,286,208	276,618	15,340,877	274,357
Diluted common shares	20,213,102	276,618	17,293,833	274,357

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statement of Redeemable Convertible Preferred Stock

(unaudited)

(amounts in thousands, except share amounts)

es B eemable vertible erred stock		Series C redeemable convertible preferred stock		Series D redeemable convertible preferred stock		Series E redeemable convertible preferred stock		Series F redeemable convertible preferred stock		Series G redeemable convertible preferred stock	
res	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amou
,511	$5,056	365,903	$6,460	1,573,126	$34,619	1,634,874	$29,130	2,701,957	$15,620	2,840,260	$27,78
	—	11,094	279	11,415	314	—	—	—	—	—	—
	—	—	—	—	—	—	139	—	207	—	641
5,511)	(5,056)	(376,997)	(6,739)	(1,584,541)	(34,933)	(1,634,874)	(29,269)	(2,701,957)	(15,827)	(2,840,260)	(28,4
	$—	—	$—	—	$—	—	$—	—	$—	—	$—

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statement of Stockholders' Equity (Deficit)

(unaudited)

(amounts in thousands, except share amounts)

	Series A convertible preferred stock		Common stock		Additional paid-in	Accumulated	Total stockholders'
	Shares	Amount	Shares	Amount	capital	deficit	equity (deficit)
Balance, December 31, 2013	66,666	$ 247	280,974	$ 1	$ -	$ (62,620)	$ (62,372)
Stock-based compensation	—	—	—	—	1,035	88	1,123
Employee stock purchase			30,358		413		413
Stock options exercised	—	—	243,828	—	229	—	229
Warrants exercised - preferred & common	—	—	92,584	—	76	—	76
Reclassification of warrant liability	—	—	—	—	22	—	22
Deemed dividend on redeemable convertible preferred stock	—	—	—	—	—	(987)	(987)
Conversion of preferred stock	(66,666)	(247)	14,259,647	14	120,484	—	120,251
Issuance of common stock in connection with initial public offering	—	—	3,529,411	3	49,841	—	49,844
Net income	—	—	—	—	—	5,307	5,307
Balance, September 30, 2014	—	$ —	18,436,802	$ 18	$ 172,100	$ (58,212)	$ 113,906

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows

(unaudited)

(amounts in thousands)

	Nine months ended September 30, 2014	2013
Cash flows from operating activities		
Net income	$5,307	$3,464
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	8,779	5,995
Loss on rental units	1,203	330
Loss on disposal of other fixed assets	—	85
Provision for sales returns	2,558	1,090
Provision for doubtful accounts	1,201	1,353
Provision for rental revenue adjustments	5,530	4,057
Provision for inventory obsolescence	125	92
Stock-based compensation expense	1,123	116
Deferred tax assets	(999)	—
Increase (decrease) in fair value of preferred stock warrant liability	(36)	202
Changes in operating assets and liabilities		
Accounts receivable	(17,119)	(9,176)
Inventories	(3,208)	(130)
Deferred costs of rental revenue	(134)	(124)
Prepaid expenses and other current assets	(449)	(404)
Accounts payable and accrued expenses	1,982	2,718
Accrued payroll	834	447
Warranty reserve	363	396
Deferred revenue	1,574	867
Income tax receivable	87	—
Income tax payable	2,647	100
Net cash provided by operating activities	11,368	11,478
Cash flows from investing activities		
Investment in intangible assets	(184)	(7)
Production of rental equipment	(10,132)	(11,918)
Purchases of property and equipment	(1,060)	(2,572)
Net cash used in investing activities	(11,376)	(14,497)
Cash flows from financing activities		
Proceeds from borrowings	6,000	6,000
Proceeds from redeemable convertible preferred stock warrants and common stock warrants exercised	467	1,875
Proceeds from stock options exercised	229	—
Proceeds from initial public offering	56,471	—

Costs associated with initial public offering	(4,942)	—
Employee stock purchase	413	—
Repayment of debt from investment in intangible assets	(130)	(159)
Repayment of borrowings	(15,861)	(2,750)
Net cash provided by financing activities	42,647	4,966
Net increase (decrease) in cash and cash equivalents	42,639	1,947
Cash and cash equivalents, beginning of period	13,521	15,112
Cash and cash equivalents, end of period	$56,160	$17,059
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	478	307
Cash paid during the period for income taxes	1,673	124
Non-cash transactions:		
Deemed dividend on redeemable convertible preferred stock	987	5,359

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 condensed 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 develops, manufactures and markets innovative oxygen concentrators used for supplemental long-term oxygen therapy by patients with chronic obstructive pulmonary disease, or COPD, and other chronic respiratory conditions. The Company's proprietary Inogen One systems are designed to address the quality-of-life and other shortcomings of the traditional oxygen therapy model, which Inogen calls the delivery model. Traditionally, oxygen therapy patients have relied upon stationary oxygen concentrator systems in the home in conjunction with regular deliveries of oxygen tanks or cylinders for ambulatory, or mobile, use, limiting their mobility and requiring them to plan activities outside of their homes around delivery schedules and a finite oxygen supply. The Company's Inogen One systems concentrate the air around them to offer a single source of supplemental oxygen anytime, anywhere from devices weighing approximately five to seven pounds. Inogen's products eliminate the need for oxygen deliveries, as well as regular use of a stationary concentrator, thereby improving patient quality-of-life and fostering patient mobility.

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, 2013 filed with the SEC on April 1, 2014 (Annual Report).

b) Use of estimates
The preparation of the Company's condensed financial statements in accordance with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the amounts reported in these condensed financial statements and accompanying 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.

c) Reclassifications

Certain reclassifications have been made to prior years financial statements to conform to current period financial statement presentation with no effect on previously reported financial position, results of operations or 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 shareholders 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 our IPO, the Company's outstanding redeemable convertible preferred stock and non-redeemable preferred stock were all converted to common stock. As of September 30, 2014, the Company had 18,436,802 shares of common stock outstanding.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

e) Revenue from contracts with customers

In May 2014, the FASB issued Accounting Standards Update No. 2014-09, Revenue from Contracts with Customers (ASU 2014-09), which supersedes nearly all existing revenue recognition guidance under U.S. 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 for 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 U.S. GAAP.

The standard is effective for annual periods beginning after December 15, 2016, and interim periods therein, using either of the following transition methods: (i) a full retrospective approach reflecting the application of the standard in each prior reporting period with the option to elect certain practical expedients, or (ii) a retrospective approach with the cumulative effect of initially adopting ASU 2014-09 recognized at the date of adoption (which includes additional footnote disclosures). The Company is currently evaluating the impact of the Company’s pending adoption of ASU 2014-09 on the Company’s consolidated financial statements and has not yet determined the method by which the Company will adopt the standard in 2017.

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 recognized upon shipment of the product. Provisions for estimated returns and discounts are made at the time of shipment. 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 of shipment.

Revenue from the sales 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 accrued $1,172 and $809 to provide for future warranty costs at September 30, 2014 and December 31, 2013, 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 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.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

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.

Revenue from the sales of used rental equipment is recognized upon delivery 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.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

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 accrual is based on historical trends and estimates of future collectability.

Fair value of financial instruments

The Company's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses, debt and warrants. The carrying values of cash and cash equivalents, 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 appropriate recognized in the respective periods.

The fair value of the Company's preferred stock warrant liability was estimated using a Monte Carlo valuation model.

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 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 following table summarizes fair value measurements by level at December 31, 2013 for the liabilities measured at fair value on a recurring basis:

	Level 1	Level 2	Level 3	Total
Preferred stock warrant liability	$ —	$ —	$ 260	$ 260
Total liabilities	$ —	$ —	$ 260	$ 260

12

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

The following table summarizes the fair value measurements using significant Level 3 inputs, and changes therein as of nine months ended September 30, 2014.

	Warrant liability
Balance as of December 31, 2013	$ 260
Fair value of preferred stock warrants exercised	(148)
Change in fair value	(36)
Reclassification of liability to additional paid in capital	(76)
Balance as of September 30, 2014	$ —

The preferred stock warrant liability was marked to market at each reporting date and the fair value was estimated using a Monte Carlo valuation model, which takes into consideration the market values of comparable public companies, considering among other factors, the use of multiples of earnings, and adjusted to reflect the restrictions on the ability of the Company's shares to trade in an active market.

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 does not allow returns from providers. 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 becoming realizable. The reserve is based on historical revenue adjustments as a percentage of rental revenue billed 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.

At September 30, 2014 and December 31, 2013, included in accounts receivable on the balance sheets were earned but unbilled receivables of $3,410 and $1,435, respectively.

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 and short-term investments to date.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Concentration of customers and vendors

The Company sells its products to home medical equipment providers in the United States and in foreign countries on a credit basis. No single customer represented more than 10% of the Company's total revenue for the nine months ended September 30, 2014 and September 30, 2013. No single customer represented more than 10% of the Company's total accounts receivable balance as of September 30, 2014, or as of December 31, 2013.

The Company also rents products directly to patients, which resulted in a customer concentration relating to Medicare's service reimbursement programs. Medicare's service reimbursement programs (net of patient co-insurance obligations) accounted for 78.6% and 70.8% of rental revenue for the three months ended September 30, 2014 and September 30, 2013, respectively, and based on total revenue were 26.7% and 27.4% for the three months ended September 30, 2014 and September 30, 2013, respectively. Medicare's service reimbursement programs (net of patient co-insurance obligations) accounted for 74.3% and 73.1% of rental revenue for the nine months ended September 30, 2014 and September 30, 2013, respectively, and based on total revenue were 25.6% and 28.8% for the nine months ended September 30, 2014 and September 30, 2013, respectively. Accounts receivable balances relating to Medicare's service reimbursement programs amounted to $3,661 or 20.3% of total accounts receivable at September 30, 2014 as compared to $2,560, or 25.0% of total accounts receivable at December 31, 2013.

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, 2014, the Company's three major vendors accounted for 18.8%, 17.8%, and 8.0%, respectively, of total raw material purchases. For the nine months ended September 30, 2013, the Company's three major vendors accounted for 15.7%, 14.9% and 8.6%, respectively, of total raw material purchases.

A portion of revenue is earned from sales outside the United States. Non-U.S. revenue is denominated in U.S. dollars. 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, 2014 and September 30, 2013 is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
U.S. revenue	$22,571	$15,194	$65,996	$42,768
Non-U.S. revenue	6,822	4,583	17,423	12,913
Total revenue	$29,393	$19,777	$83,419	$55,681

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, 2014	December 31, 2013
Raw materials and work-in-progress	$ 6,058	$ 3,783
Finished goods	1,456	565
Less: reserves	(183)	(100)
Inventories	$ 7,331	$ 4,248

14

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

(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	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

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 $367 and $251 for the three months ended September 30, 2014 and September 30, 2013, respectively, and $1,157 and $707 for the nine months ended September 30, 2014 and September 30, 2013, 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 September 30, 2014 and September 30, 2013, respectively, and the nine months ended September 30, 2014 and September 30, 2013, respectively.

	Three Months Ended September 30,		Nine Months Ended September 30,	
Depreciation and amortization	2014	2013	2014	2013
Rental equipment	$2,752	$1,955	$7,512	$4,921
Other property and equipment	396	319	1,142	871
Total depreciation and amortization	$3,148	$2,274	$8,654	$5,792

Property and equipment and rental equipment with associated accumulated depreciation is summarized below for September 30, 2014 and December 31, 2013, respectively.

	September 30, 2014	December 31, 2013
Property and equipment		
Rental equipment, net of allowance	$ 45,532	$ 37,573
Other property and equipment	9,165	8,105
Property and equipment	54,697	45,678
Accumulated depreciation		
Rental equipment	19,087	12,545
Other property and equipment	4,553	3,411
Accumulated depreciation	23,640	15,956
Net property and equipment		
Rental equipment	26,445	25,028
Other property and equipment	4,612	4,694
Property and equipment, net	$ 31,057	$ 29,722

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

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 three months and six months 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.

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.

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.

Stock split

On November 11, 2013, the Company's board of directors and stockholders approved a 3:1 reverse stock split. This became effective as of November 12, 2013 and the effect of this event has been reflected in all of the share quantities and per share amounts throughout these financial statements. The shares of common stock retained a par value of $0.001.

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, redeemable convertible preferred stock and preferred stock warrants, 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.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

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. Further, as the Company's holders of redeemable convertible preferred stock have the right to participate in any dividend declared on the Company's common stock, basic and diluted EPS are potentially subject to computation using the two-class method, under which the Company's undistributed earnings are allocated amongst the holders of common and redeemable convertible preferred stock.

On February 20, 2014, the Company completed an initial public offering (IPO) of 4,411,763 shares of common stock at a price of $16.00 per share. The Company sold 3,529,411 shares of common stock and certain stockholders sold 882,352 shares of common stock. As of March 7, 2014 the underwriters elected to purchase 99,550 additional shares of common stock at the IPO price from the certain selling shareholders. All redeemable convertible preferred stock and non-redeemable preferred stock-outstanding as of the IPO automatically converted into 14,259,647 shares of common stock.

The computation of EPS is as follows:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2014	2013	2014	2013
Numerator—basic:				
Net income	$2,133	$774	$5,307	$3,464
Less deemed dividend on redeemable convertible preferred stock	-	(1,851)	(987)	(5,359)
Net income (loss) before preferred rights dividend	2,133	(1,077)	4,320	(1,895)
Less preferred rights dividend	-	-	-	-
Less: undistributed earnings to preferred stock	-	-	(563)	-
Net income (loss) attributable to common stockholders - basic	$2,133	$(1,077)	$3,757	$(1,895)
Numerator—diluted:				
Net income	$2,133	$774	$5,307	$3,464
Less deemed dividend on redeemable convertible preferred stock	-	(1,851)	(987)	(5,359)
Net income (loss) before preferred rights dividend	2,133	(1,077)	4,320	(1,895)
Less undistributed earnings to preferred stock	-	-	(507)	-
Net income (loss) attributable to common stockholders - diluted	$2,133	$(1,077)	$3,813	$(1,895)
Denominator:				
Weighted-average common shares - basic common stock	18,286,208	276,618	15,340,877	274,357
Weighted-average common shares - diluted common stock	20,213,102	276,618	17,293,833	274,357
Net income (loss) per share - basic common stock	$0.12	$(3.90)	$0.24	$(6.91)

Net income (loss) per share - diluted common stock	$0.11	$(3.90)	$0.22	$(6.91)

The computations of diluted net income applicable to common shareholders exclude redeemable convertible preferred stock, warrants and common stock options which were anti-dilutive for the three months and nine months ended September 30, 2013. There were no anti-dilutive instruments for the three and nine months ended September 30, 2014.

3. Intangible assets

During the year ended December 31, 2008, the Company acquired Comfort Life Medical, LLC (Comfort Life). 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 September 30, 2014 and December 31, 2013, 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 for the three and nine months ended September 30, 2014 and September 30, 2013. The Company recalculated interest and amortization of the period based on adjusted asset and debt.

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

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

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 nine months ended September 30, 2014 and September 30, 2013, 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 three months and nine months ended September 30, 2014, the Company paid $4 and $184 for its patient setup video, website development and redesign and production of commercials. The Company did not capitalize any intangible assets during the three and nine months ended September 30, 2013.

Amortization expense for intangible assets for the three months ended September 30, 2014 and September 30, 2013 was $45 and $68 respectively, and for the nine months ended September 30, 2014 and September 30, 2013 was $125 and $203, respectively.

The following tables represent the changes in net carrying values of the intangibles as of the respective dates:

September 30, 2014	Average estimated useful lives (in years)	Gross carrying amount	Accumulated amortization	Net amount
Licenses	10	$ 185	$ 77	$ 108
Patents and websites	5	873	737	136
Commercial	2	107	77	30
Total		$ 1,165	$ 891	$ 274

December 31, 2013	Average estimated useful lives (in years)	Gross carrying amount	Accumulated amortization	Net amount
Licenses	10	$ 185	$ 63	$ 122

Patents	5	723	662	61
Commercial	2	73	41	32
Total		$ 981	$ 766	$ 215

4. Long-term debt

Amended and restated credit and term loan agreement

On October 12, 2012, the Company entered into an amended and restated credit and term loan agreement with its current lenders whereby the existing balances and the payback terms were not changed. This transaction did not result in any debt extinguishment losses or gains. The Company did not incur or defer any financing cost directly related to the amendment of the credit and term loan agreement. Due to the completion of the IPO during the term of this facility, a fee equal to 1% of the facility amount of $120, was paid to the lenders in March of 2014, and was included in general and administrative expenses in the Company's Statements of Operations for the quarter ended March 31, 2014.

The amended and restated credit and term loan agreement with the Company's current lenders provided for new borrowings of up to $12,000 secured by substantially all of the Company's assets. The amended and restated credit and term loan agreement provided for the existing term loan facility for rental assets amounting to up to $3,000 (Term Loan A), a term loan facility for rental assets amounting to up to $8,000 (Term Loan B), a new term loan facility for rental assets amounting to up to $12,000 (Term Loan C), and an accounts receivable revolving line of credit amounting to up to $1,000 based on 80% of eligible accounts receivable, as defined (AR Revolver).

Principal and interest amounts for all the term loans were payable monthly. Each term loan bore interest at the Base Rate, which is a rate equal to the applicable margin plus the greater of (i) the prime rate, (ii) the federal funds effective rate, as defined in the agreement, plus 1% and (iii) the daily adjusting LIBOR rate, plus 1%. The applicable margins for Term Loans A, B, and C were 1.25%, 2.5% and 2.25%, respectively.

The Term Loan A facility of $3,000 is presented net of principal payments that began in May 2011. The net balances of this term loan facility were $0 and $417 as of September 30, 2014 and December 31, 2013, respectively.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

The Term Loan B facility for $8,000 is presented net of principal payments that began in May 2012. The net balances of this term loan facility were $0 and $3,778 as of September 30, 2014 and December 31, 2013, respectively.

The Term Loan C facility for $12,000 is presented net of principal payments that began in November 2013. The net balances were $0 and $5,666 as of September 30, 2014 and December 31, 2013, respectively.

The AR Revolver expired on October 13, 2013, and was not renewed by the Company. There were no borrowings under the AR Revolver as of and during the nine months ended September 30, 2014.

The interest rates were 4.5% for Term Loan A, 5.75% for Term Loan B, and 5.5% for Term Loan C at September 30, 2014 and December 31, 2013. As of September 30, 2014 and December 31, 2013, the Company was in compliance with all covenants of the amended and restated credit and term loan agreement.

The Company paid all outstanding balances and accrued interest on the term loan agreements on August 22, 2014 totaling $11,600.

	September 30, 2014	December 31, 2013
Term Loan A, bearing interest at Base Rate, monthly payments of $83 beginning May 2011 through April 2014	$ —	$ 417
Term Loan B, bearing interest at Base Rate, monthly payments of $222 beginning May 2012 through April 2015	—	3,778
Term Loan C bearing interest at Base Rate, monthly payments of $167 beginning November 2013 through May 2014, $367 a month beginning June 2014 through October 2016.	—	5,666
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	658	788
Subtotal	$ 658	$ 10,649
Less: current maturities	(267)	(5,258)

Long-term debt, net of current portion	$ 391	$ 5,391

As of September 30, 2014, the minimum aggregate payments due under non-cancelable debt are summarized as follows:

	September 30, 2014
Remaining 3 months of 2014	$ 44
2015	299
2016	315
Total	$ 658

5. Commitments and contingencies

Leases

The Company leases its offices and certain equipment under operating leases that expire through December 2019. At September 30, 2014, the minimum aggregate payments due under non-cancelable leases are summarized as follows:

	September 30, 2014
Remaining three months of 2014	$ 214
2015	738
2016	336
2017	328
2018	315
Thereafter	313
	$ 2,244

Rent expense of $182 and $223, for the three months ended September 30, 2014 and September 30, 2013, respectively, and $569 and $690 for the nine months ended September 30, 2014 and September 30, 2013, respectively was included in the accompanying Statements of Operations.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Warranty obligation

The following table identifies the changes in the Company's aggregate product warranty liabilities for the nine and twelve month periods ended September 30, 2014 and December 31, 2013, respectively:

	September 30, 2014	December 31, 2013
Product warranty liability at beginning of period	$ 809	$ 447
Accruals for warranties issued	814	533
Adjustments related to preexisting warranties (including changes in estimates)	296	322
Settlements made (in cash or in kind)	(747)	(493)
Product warranty liability at end of period	$ 1,172	$ 809

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 is 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.

Amended & restated employment agreements

On October 1, 2013, the Company entered into an Employment Agreement with the Chief Executive Officer (CEO) including considerations for salary, bonus awards, and severance and change of control benefits upon certain qualifying terminations up to a period of thirty-six months.

On October 1, 2013, the Company entered into employment agreements with certain key employees including considerations for salary, bonus awards, and severance and change of control benefits for a period up to twenty-four months upon certain qualifying terminations.

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 our patents. The case, Inogen Inc. v. Inova Labs Inc., Case No. 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 attorneys' 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

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

alleging patent invalidity, non-infringement and inequitable conduct. The Company denied the allegations in the Defendant's counterclaims and 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 our motion to dismiss the Defendant's inequitable conduct counterclaim.

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. At this time, the Company does not anticipate that any of these proceedings will have a material adverse effect on our business.

6. Income taxes

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. The Company does not expect any material changes to unrecognized tax benefits in the next 12 months, and has not incurred any tax related penalties or interest.

Income tax expense was $1,341 and $3,408, an effective tax rate of 38.6% and 39.1%, for the three and nine months ended September 30, 2014, respectively, compared to $43 and $151, an effective tax rate of 5.3% and 4.2% for the comparable periods ended September 30, 2013, respectively. The variation in the tax rate year-over-year was primarily driven by the change in the Company's deferred tax asset valuation allowance. As of September 30, 2013, the Company maintained a full valuation allowance against its federal and state deferred tax assets which significantly reduced the Company's effective tax rate. In December of 2013, the Company evaluated its facts and circumstances and concluded that it was appropriate to release $22,909 of the valuation allowance which created a one-time tax benefit of $21,587 for the year ended December 31, 2013. Refer to the Company's 2013 10-K filing for additional information regarding the deferred tax asset valuation allowance. Variations in the tax rate year-over-year were also due to an increase in permanent tax differences related to employee stock option expense.

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.

7. Convertible preferred stock

All outstanding preferred stock automatically converted into common stock in connection with the closing of the IPO. At the closing of the IPO, 9,564,140 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. There was no outstanding preferred stock as of September 30, 2014.

The Company's Series C preferred stock warrants expired in connection with the IPO. As of February 20, 2014, 2,756 Series C preferred stock warrants were forfeited and cancelled since they were not exercised prior to the IPO.

On February 20, 2014, the Company's Thirteenth Amended and restated Certificate of Incorporation came in to effect which authorized the Company to issue 10,000,000 of preferred stock. As of September 30, 2014 there was no preferred stock outstanding.

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

A summary of the terms of the various types of redeemable convertible preferred stock at December 31, 2013 is as follows:

Redeemable convertible preferred stock as of December 31, 2013 (1)							
Series	B	C	D	E	F	G	Total
Shares authorized	500,000	400,000	1,700,000	1,700,000	2,800,000	2,900,000	10,000,000
Shares issued	425,511	365,903	1,573,126	1,634,874	2,701,957	2,840,260	9,541,631
Par value	$0.001	$0.001	$0.001	$0.001	$0.001	$0.001	
Conversion rate	1.45108	1.73014	1.87951	2.69244	1.0000	1.0000	
Liquidation preference per share	$11.880	$17.580	$21.900	$19.224	$7.140	$14.083	
Dividend rate	5 %	8 %	8 %	8 %	8 %	8 %	
			July	October			