

Inogen Inc
Form 10-Q
August 12, 2014

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 June 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
(State or other jurisdiction of
incorporation or organization)

33-0989359
(I.R.S. Employer
Identification No.)

326 Bollay Drive
Goleta, California

93117

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(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 Smaller reporting company
(Do not check if a smaller reporting company)

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

The total number of shares of common stock outstanding as of July 31, 2014 was 18,240,043.

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INOGEN, INC.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS.

Inogen, Inc.

Balance Sheets

(unaudited)

(amounts in thousands)

	June 30, 2014	December 31, 2013
Assets		
Current assets		
Cash and cash equivalents	\$69,046	\$ 13,521
Accounts receivable, net of allowances of \$4,139 and \$3,390 at June 30, 2014 and December 31, 2013, respectively	15,645	10,231
Inventories, net of allowances of \$152 and \$100 at June 30, 2014 and December 31, 2013, respectively	6,101	4,248
Deferred cost of rental revenue	431	289
Income tax receivable	-	87
Deferred tax asset-current	5,345	3,923
Prepaid expenses and other current assets	1,126	531
Total current assets	97,694	32,830
Property and equipment		
Rental equipment, net of allowances of \$682 and \$157 at June 30, 2014 and December 31, 2013, respectively	42,859	37,573
Manufacturing equipment and tooling	2,641	2,551
Computer equipment and software	3,508	2,973
Furniture and equipment	604	601
Leasehold improvements	888	887
Construction in process	1,067	1,093
Total property and equipment	51,567	45,678
Less accumulated depreciation	(20,917)	(15,956)
Property and equipment, net	30,650	29,722
Intangible assets, net	315	215
Deferred tax asset - noncurrent	16,727	17,865
Other assets	80	1,765

Total assets

\$145,466 \$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)

	June 30, 2014	December 31, 2013
Liabilities, redeemable convertible preferred stock and stockholders' equity (deficit)		
Current liabilities		
Accounts payable and accrued expenses	\$12,355	\$9,219
Accrued payroll	2,841	2,898
Current portion of long-term debt	7,080	5,258
Warranty reserve	605	420
Deferred revenue	1,984	1,487
Income tax payable	1,435	-
Total current liabilities	26,300	19,282
Long-term liabilities		
Warranty reserve-noncurrent	473	389
Preferred stock warrant liability	-	260
Deferred revenue-noncurrent	1,546	776
Long-term debt, net of current portion	6,333	5,391
Total liabilities	34,652	26,098
Commitments and contingencies (Note 5)		
Redeemable convertible preferred stock		
Preferred stock, \$0.001 par value per share; 10,000,000 shares authorized; 0 and 9,541,631 shares issued and outstanding; liquidation preference of \$0 and \$136,660 at June 30, 2014 and December 31, 2013, respectively	-	118,671
Stockholders' equity (deficit)		
Preferred stock, \$0.001 par value per share; 100,000 shares authorized; 0 and 66,666 shares issued and outstanding; liquidation preference of \$0 and \$250 at June 30, 2014 and December 31, 2013, respectively	-	247
Common stock, \$0.001 par value per share; 60,000,000 shares authorized for both periods; 18,240,043 and 280,974 shares issued and outstanding at June 30, 2014 and December 31, 2013, respectively	18	1
Additional paid-in-capital	171,141	-
Accumulated deficit	(60,345)	(62,620)
Total stockholders' equity (deficit)	110,814	(62,372)
Total liabilities, redeemable convertible preferred stock and stockholders' equity (deficit)	\$145,466	\$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		Six months ended June	
	June 30,	2013	30,	2013
	2014		2014	
Revenue				
Sales revenue	\$20,464	\$12,751	\$35,321	\$21,646
Rental revenue	9,929	7,406	18,705	14,258
Total revenue	30,393	20,157	54,026	35,904
Cost of revenue				
Cost of sales revenue	10,682	6,464	18,223	11,655
Cost of rental revenue, including depreciation of \$2,503 and \$1,624 for the three months ended and \$4,760 and \$2,966 for the six months ended, respectively	4,597	2,636	8,751	5,075
Total cost of revenue	15,279	9,100	26,974	16,730
Gross profit	15,114	11,057	27,052	19,174
Operating expenses				
Research and development	879	640	1,514	1,143
Sales and marketing	6,364	4,595	12,069	8,742
General and administrative	3,908	3,430	7,957	6,264
Total operating expenses	11,151	8,665	21,540	16,149
Income from operations	3,963	2,392	5,512	3,025
Other income (expense)				
Interest expense	(203)	(95)	(336)	(199)
Interest income	12	3	18	6
Change in fair value of preferred stock warrant liability	-	(263)	36	(243)
Other income	4	-	11	209
Total other expense, net	(187)	(355)	(271)	(227)
Income before provision for income taxes	3,776	2,037	5,241	2,798
Provision for income taxes	1,490	77	2,067	108
Net income	\$2,286	\$1,960	\$3,174	\$2,690
Less deemed dividend on redeemable convertible preferred stock	-	(1,785)	(987)	(3,508)
Net income (loss) before preferred rights dividend	\$2,286	\$175	\$2,187	\$(818)
Less preferred rights dividend on redeemable convertible preferred stock	-	(175)	-	-
Net income (loss) after deemed dividend	\$2,286	\$-	\$2,187	\$(818)
Basic net income (loss) per share attributable to common stockholders (note 2)	\$0.13	\$-	\$0.13	\$(2.98)
Diluted net income (loss) per share attributable to common stockholders (note 2)	\$0.11	\$-	\$0.11	\$(2.98)

Weighted-average number of shares used in calculating income
(loss) per share attributable to common stockholders (note 2):

Basic common shares	18,201,661	274,487	13,843,803	274,396
Diluted common shares	20,146,915	274,487	15,826,754	274,396

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Redeemable Convertible Preferred Stock

(unaudited)

(amounts in thousands, except share amounts)

Series B redeemable convertible preferred stock Shares	Amount	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	
		Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount	Shares	Amount
5,511	\$5,056	365,903	\$6,460	1,573,126	\$34,619	1,634,874	\$29,130	2,701,957	\$15,620	2,840,260	\$27,700
	—	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)	(28,400)
	\$—	—	\$—	—	\$—	—	\$—	—	\$—	—	\$—

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Stockholders' Equity (Deficit)

(unaudited)

(amounts in thousands, except share amounts)

	Series A convertible preferred stock		Common stock		Additional paid-in capital	Accumulated deficit	Total stockholders' equity (deficit)
	Shares	Amount	Shares	Amount			
Balance, December 31, 2013	66,666	\$ 247	280,974	\$ 1	\$ -	\$ (62,620)	\$ (62,372)
Stock-based compensation	—	—	—	—	578	88	666
Stock options exercised	—	—	93,414	—	109	—	109
Warrants exercised - preferred & common	—	—	76,597	—	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	49,872	—	49,875
Net income	—	—	—	—	—	3,174	3,174
Balance, June 30, 2014	—	\$ —	18,240,043	\$ 18	\$ 171,141	\$ (60,345)	\$ 110,814

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows

(unaudited)

(amounts in thousands)

	Six months ended June 30,	
	2014	2013
Cash flows from operating activities		
Net income	\$3,174	\$2,690
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	5,586	3,653
Loss on rental units and other fixed assets	921	168
Provision for sales returns	1,178	760
Provision for doubtful accounts	571	969
Provision for rental revenue adjustments	3,411	1,500
Provision for inventory obsolescence	79	63
Stock-based compensation expense	666	51
Deferred tax assets	(284)	—
Increase (decrease) in fair value of preferred stock warrant liability	(36)	243
Changes in operating assets and liabilities		
Accounts receivable	(10,574)	(6,376)
Inventories	(1,932)	(171)
Deferred costs of rental revenue	(142)	(37)
Prepaid expenses and other current assets	(595)	(519)
Accounts payable and accrued expenses	3,136	2,625
Accrued payroll	(57)	172
Warranty reserve	269	279
Deferred revenue	1,267	715
Income tax receivable	87	—
Income tax payable	1,435	92
Net cash provided by operating activities	8,160	6,877
Cash flows from investing activities		
Investment in intangible assets	(180)	—
Production of rental equipment	(6,752)	(7,746)
Purchases of property and equipment	(603)	(1,361)
Net cash used in investing activities	(7,535)	(9,107)
Cash flows from financing activities		
Proceeds from borrowings	6,000	2,000
Proceeds from redeemable convertible preferred stock warrants and common stock warrants exercised	467	1,231
Proceeds from stock options exercised	109	—
Proceeds from initial public offering	56,471	—
Costs associated with initial public offering	(4,911)	—

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Repayments of debt from investment in intangible assets	(86)	(106)
Repayment of borrowings	(3,150)	(1,833)
Net cash provided by financing activities	54,900	1,292
Net increase (decrease) in cash and cash equivalents	55,525	(938)
Cash and cash equivalents, beginning of period	13,521	15,112
Cash and cash equivalents, end of period	\$69,046	\$14,174
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	317	212
Cash paid during the period for income taxes	802	60
Non-cash transactions:		
Deemed dividend on redeemable convertible preferred stock	987	3,508

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 June 30, 2014, the Company had 18,240,043 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 \$1,078 and \$809 to provide for future warranty costs at June 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 appropriately 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

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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

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 ended June 30, 2014 and December 31, 2013, respectively.

	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 June 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 June 30, 2014 and December 31, 2013, included in accounts receivable on the balance sheets were earned but unbilled receivables of \$2,729 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 six months ended June 30, 2014 and June 30, 2013. No single customer represented more than 10% of the Company's total accounts receivable balance as of June 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 71.7% and 73.3% of rental revenue for the three months ended June 30, 2014 and June 30, 2013, respectively, and based on total revenue were 23.4% and 26.9% for the three months ended June 30, 2014 and June 30, 2013, respectively. Medicare's service reimbursement programs (net of patient co-insurance obligations) accounted for 72.1% and 74.3% of renta