

Inogen Inc
Form 10-Q
August 04, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 2016

OR

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

For the Transition Period From _____ to _____

Commission file number: 001-36309

INOGEN, INC.

(Exact name of registrant as specified in its charter)

Delaware	33-0989359
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

326 Bollay Drive	
Goleta, California	93117
(Address of principal executive offices)	(Zip Code)
(805) 562-0500	

(Registrant's telephone number, including area code)

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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

As of July 29, 2016, the registrant had 20,095,609 shares of common stock, par value \$0.001, outstanding.

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INOGEN, INC.

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Inogen, Inc.

Balance Sheets

(unaudited)

(amounts in thousands)

	June 30, 2016	December 31, 2015
Assets		
Current assets		
Cash and cash equivalents	\$84,500	\$66,106
Short-term investments	13,616	16,793
Accounts receivable, net	27,837	19,872
Inventories, net	12,514	8,648
Deferred cost of revenue	503	397
Income tax receivable	1,228	2,158
Prepaid expenses and other current assets	2,363	870
Total current assets	142,561	114,844
Property and equipment		
Rental equipment, net	55,074	54,677
Manufacturing equipment and tooling	5,640	4,680
Computer equipment and software	4,686	4,503
Furniture and equipment	802	732
Leasehold improvements	1,091	978
Land and building	125	125
Construction in process	478	578
Total property and equipment	67,896	66,273
Less accumulated depreciation	(39,456)	(35,593)
Property and equipment, net	28,440	30,680
Intangible assets, net	184	229
Deferred tax asset - noncurrent	11,504	15,464
Other assets	97	97
Total assets	\$182,786	\$161,314

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Balance Sheets (continued)

(unaudited)

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

	June 30, 2016	December 31, 2015
Liabilities and stockholders' equity		
Current liabilities		
Accounts payable and accrued expenses	\$ 19,298	\$ 12,867
Accrued payroll	4,528	5,271
Current portion of long-term debt	159	315
Warranty reserve - current	1,674	1,226
Deferred revenue - current	2,318	2,323
Income tax payable	—	11
Total current liabilities	27,977	22,013
Long-term liabilities		
Warranty reserve - noncurrent	1,347	747
Deferred revenue - noncurrent	5,619	4,199
Other noncurrent liabilities	340	337
Total liabilities	35,283	27,296
Commitments and contingencies (Note 9)		
Stockholders' equity		
Common stock, \$0.001 par value per share; 200,000,000 authorized; 20,068,955 and 19,782,403		
shares issued and outstanding as of June 30, 2016 and December 31, 2015, respectively	20	20
Additional paid-in capital	185,086	179,143
Accumulated deficit	(37,601)	(45,108)
Accumulated other comprehensive loss	(2)	(37)
Total stockholders' equity	147,503	134,018
Total liabilities and stockholders' equity	\$ 182,786	\$ 161,314

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Comprehensive Income

(unaudited)

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

	Three months ended		Six months ended	
	June 30,	2015	June 30,	2015
	2016		2016	2015
Revenue				
Sales revenue	\$45,578	\$32,385	\$78,389	\$55,434
Rental revenue	8,989	11,644	19,167	22,347
Total revenue	54,567	44,029	97,556	77,781
Cost of revenue				
Cost of sales revenue	23,046	17,866	39,553	30,455
Cost of rental revenue, including depreciation of \$2,908 and \$2,944 for the				
three months ended and \$5,855 and \$5,900 for the six months ended,				
respectively	5,306	5,341	10,509	10,481
Total cost of revenue	28,352	23,207	50,062	40,936
Gross profit				
Gross profit-sales revenue	22,532	14,519	38,836	24,979
Gross profit-rental revenue	3,683	6,303	8,658	11,866
Total gross profit	26,215	20,822	47,494	36,845
Operating expense				
Research and development	1,379	975	2,547	1,838
Sales and marketing	9,576	7,567	18,541	14,491
General and administrative	7,241	6,935	15,110	12,653
Total operating expense	18,196	15,477	36,198	28,982
Income from operations	8,019	5,345	11,296	7,863
Other income (expense)				
Interest expense	(2)	(6)	(5)	(13)
Interest income	36	26	65	38
Other income (expense)	(11)	(51)	86	(156)
Total other income (expense), net	23	(31)	146	(131)
Income before provision for income taxes	8,042	5,314	11,442	7,732
Provision for income taxes	2,900	1,855	3,935	2,701
Net income	5,142	3,459	7,507	5,031
Other comprehensive income, net of tax				
Unrealized gain (losses) on foreign currency hedging during the period	63	—	(35)	—
	44	—	50	—

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Add: reclassification adjustment for losses included in net income				
Total unrealized gain on foreign currency hedging	107	—	15	—
Unrealized gain on available-for-sale investments during the period	9	—	20	—
Total other comprehensive income, net of tax	116	—	35	—
Comprehensive income	\$5,258	\$3,459	\$7,542	\$5,031
Basic net income per share attributable to common stockholders (Note 5)				
	\$0.26	\$0.18	\$0.38	\$0.26
Diluted net income per share attributable to common stockholders (Note 5)				
	\$0.25	\$0.17	\$0.36	\$0.24
Weighted-average number of shares used in calculating net income per				
share attributable to common stockholders:				
Basic common shares	19,972,395	19,310,064	19,900,032	19,239,218
Diluted common shares	20,925,613	20,672,414	20,860,878	20,617,342

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statement of Stockholders' Equity

(unaudited)

(amounts in thousands, except share amounts)

	Common stock		Additional paid-in	Accumulated deficit	Accumulated other comprehensive income (loss)	Total stockholders' equity
	Shares	Amount	capital			
Balance, December 31, 2014	19,059,364	\$ 19	\$ 174,824	\$ (56,693)	\$ —	\$ 118,150
Stock-based compensation	—	—	1,327	—	—	1,327
Employee stock purchases	18,551	—	342	—	—	342
Excess tax benefits from stock-based compensation						
agreements	—	—	2,688	—	—	2,688
Stock options exercised	268,228	—	379	—	—	379
Net income	—	—	—	5,031	—	5,031
Balance, June 30, 2015	19,346,143	\$ 19	\$ 179,560	\$ (51,662)	\$ —	\$ 127,917
Balance, December 31, 2015	19,782,403	20	179,143	(45,108)	(37)	134,018
Stock-based compensation	—	—	3,451	—	—	3,451
Employee stock purchases	17,724	—	500	—	—	500
Stock options exercised	268,828	—	1,992	—	—	1,992
Net income	—	—	—	7,507	—	7,507
Other comprehensive income	—	—	—	—	35	35
Balance, June 30, 2016	20,068,955	\$ 20	\$ 185,086	\$ (37,601)	\$ (2)	\$ 147,503

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Statements of Cash Flows

(unaudited)

(amounts in thousands)

	Six months ended June 30,	
	2016	2015
Cash flows from operating activities		
Net income	\$7,507	\$5,031
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,874	6,908
Loss on rental units and other fixed assets	567	648
Gain on sale of former assets	(203)	—
Provision for sales returns and doubtful accounts	5,053	2,409
Provision for rental revenue adjustments	5,470	4,286
Provision for inventory obsolescence and other inventory losses, net of recoveries	108	113
Stock-based compensation expense	3,451	1,327
Deferred tax assets	3,960	—
Excess tax benefits from stock-based compensation arrangements	—	(2,688)
Changes in operating assets and liabilities:		
Accounts receivable	(18,436)	(12,111)
Inventories	(4,980)	(1,805)
Deferred cost of revenue	(106)	55
Income tax receivable	930	2,669
Prepaid expenses and other current assets	(1,493)	(601)
Accounts payable and accrued expenses	6,383	5,923
Accrued payroll	(743)	191
Warranty reserve	1,048	491
Deferred revenue	1,415	941
Income tax payable	(11)	—
Other noncurrent liabilities	3	(36)
Net cash provided by operating activities	16,797	13,751
Cash flows from investing activities		
Purchases of available-for-sale investments	(14,857)	(20,557)
Maturities of available-for-sale investments	18,054	6,317
Investment in intangible assets	—	(11)
Investment in property and equipment	(4,183)	(7,760)
Proceeds from sale of former assets	298	—
Net cash used in investing activities	(688)	(22,011)

(continued on next page)

See accompanying condensed notes to the financial statements.

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Inogen, Inc.

Statements of Cash Flows (continued)

(unaudited)

(amounts in thousands)

	Six months ended June 30,	
	2016	2015
Cash flows from financing activities		
Proceeds from stock options exercised	1,992	379
Proceeds from employee stock purchases	500	342
Repayment of debt from investment in intangible assets	(156)	(163)
Excess tax benefits from stock-based compensation arrangements	—	2,688
Net cash provided by financing activities	2,336	3,246
Effect of exchange rates on cash	(51)	—
Net increase (decrease) in cash and cash equivalents	18,394	(5,014)
Cash and cash equivalents, beginning of period	66,106	56,836
Cash and cash equivalents, end of period	\$84,500	\$51,822
Supplemental disclosures of cash flow information		
Cash paid during the period for interest	\$7	\$15
Cash paid (received) during the period for income taxes, net of refunds received	(927)	33

See accompanying condensed notes to the financial statements.

Inogen, Inc.

Condensed Notes to the Financial Statements

(unaudited)

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

1. Business overview

Inogen, Inc. (Company or Inogen) was incorporated in Delaware on November 27, 2001. The Company is a medical technology company that primarily develops, manufactures and markets innovative portable oxygen concentrators used to deliver supplemental long-term oxygen therapy to patients suffering from chronic respiratory conditions. Traditionally, these patients have relied on stationary oxygen concentrator systems for use in the home and oxygen tanks or cylinders for mobile use, which the Company calls the delivery model. The tanks and cylinders must be delivered regularly and have a finite amount of oxygen, which requires patients to plan activities outside of their homes around delivery schedules and a finite oxygen supply. Additionally, patients must attach long, cumbersome tubing to their stationary concentrators simply to enable mobility within their homes. The Company's proprietary Inogen One® systems concentrate the air around the patient to offer a single source of supplemental oxygen anytime, anywhere with a portable device weighing 2.8, 4.8 or 7.0 pounds with a single battery. The Company's Inogen One G4™, Inogen One G3 and Inogen One G2® have up to 3, 4.5 and 5 hours of battery life, respectively, with a single battery and can be plugged into an outlet when at home, in a car, or in a public place with outlets available. The Company's Inogen One systems reduce the patient's reliance on stationary concentrators and scheduled deliveries of tanks with a finite supply of oxygen, thereby improving patient quality of life and fostering mobility.

Portable oxygen concentrators represented the fastest-growing segment of the Medicare oxygen therapy market between 2012 and 2014. The Company estimates based on 2014 Medicare data that patients using portable oxygen concentrators represent approximately 6% to 8% of the total addressable oxygen market in the United States, although the Medicare data does not account for cash-pay sales into the market. Based on 2014 industry data, the Company believes it was the leading worldwide manufacturer of portable oxygen concentrators, as well as the largest provider of portable oxygen concentrators to Medicare patients, as measured by dollar volume. The Company believes it is the only manufacturer of portable oxygen concentrators that employs a direct-to-consumer strategy in the United States, meaning the Company markets its products to patients, processes their physician paperwork, provides clinical support as needed and bills Medicare or insurance on their behalf. To pursue a direct-to-consumer strategy, the Company's manufacturing competitors would need to meet national accreditation and state-by-state licensing requirements and secure Medicare billing privileges, as well as compete with the home medical equipment providers that many rely on across their entire homecare business.

Since adopting the Company's direct-to-consumer strategy in 2009 following its acquisition of Comfort Life Medical Supply, LLC, which had an active Medicare billing number but few other assets and limited business activities, the Company has directly sold or rented its Inogen oxygen concentrators to more than 170,000 patients as of June 30, 2016.

2. Basis of presentation and summary of significant accounting policies

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

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

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Management bases these estimates and assumptions upon historical experience, existing and known circumstances, authoritative accounting pronouncements and other factors that management believes to be reasonable. Significant areas requiring the use of management estimates relate to revenue recognition, inventory and rental asset valuations and write-downs, accounts receivable allowances for bad debts, returns and adjustments, stock compensation expense, impairment assessments, depreciation and amortization, income tax provision and uncertain tax positions, fair value of financial instruments, and fair values of acquired intangibles. Actual results could differ materially from these estimates.

Reclassifications

Certain reclassifications have been made to prior years' financial statements to conform to current period financial statements' presentation with no effect on previously reported financial position, results of operations or cash flows. These changes consisted of reclassifications to certain line items in the accompanying Statement of Cash Flows and did not change total operating, financing or investing activities as previously reported.

Recent accounting pronouncements

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

Revenue recognition pronouncements:

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU No. 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU No. 2014-09 defines a five step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing U.S. GAAP.

In August 2015, the FASB decided to delay the effective date of ASU No. 2014-09 by one year. The FASB also agreed to allow entities to choose to adopt the standard as of the original effective date. As such, the updated standard

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

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

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

In May, 2016, the FASB issued ASU No. 2016-10, Revenue with Contracts with Customers: Narrow-scope Improvements and Practical Expedients, which is an amendment to ASU No. 2014-09 that clarifies the objective of the collectability criterion, to allow entities to exclude amounts collected from customers from all sales taxes from the transaction price, to specify the measurement date

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

for noncash consideration is contract inception, variable consideration guidance applies only to variability resulting from reasons other than the form of the consideration, and clarification on contract modifications at transition. The implementation guidelines follow ASU No. 2014-09.

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

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

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

Business segments

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

3. Fair value of financial instruments

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

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

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Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

Fair value accounting

Accounting Standards Codification (ASC) 820—Fair Value Measurements and Disclosures, creates a single definition of fair value, establishes a framework for measuring fair value in U.S. GAAP and expands disclosures about fair value measurements. ASC 820 emphasizes that fair value is a market-based measurement, not an entity-specific measurement, and states that a fair value measurement is to estimate the price at which an orderly transaction to sell an asset or to transfer the liability would take place between market participants at the measurement date under current market conditions. Assets and liabilities adjusted to fair value in the balance sheet are categorized based upon the level of judgment associated with the inputs used to measure their fair value. Level inputs, as defined by ASC 820, are as follows:

Level input	Input definition
-------------	------------------

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

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

Inogen, Inc.

Condensed Notes to the Financial Statements (continued)

(unaudited)

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

The following table summarizes fair value measurements by level for the assets measured at fair value on a recurring basis for cash, cash equivalents and short-term investments:

	As of June 30, 2016			Cash and cash equivalents	Short- term investments
	Adjusted cost	Gross unrealized losses	Fair value		
Cash	\$42,290	\$ —	\$42,290	\$ 42,290	\$ —
Level 1:					
Money market accounts	33,270	—	33,270	33,270	—
Level 2:					
Certificates of deposit	22,559	(3)	22,556	8,940	13,616