Inogen Inc
Form 10-K
April 01, 2014
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the Fiscal Year Ended December 31, 2013

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)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock, $0.001 par value	**The NASDAQ Global Select Market**

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No x

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 x

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 ¨

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405 of this chapter) is not contained herein, and will not be contained, to the best of the Registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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 ¨ No x

As of June 30, 2013, the last business day of the registrant s most recently completed second fiscal quarter, the registrant s common stock was not listed on any exchange or over-the-counter market. The registrant s common stock began trading on the NASDAQ Global Select Market on February 14, 2014. The aggregate market value of Inogen, Inc. voting and non-voting common equity held by non-affiliates as of February 28, 2014, based on the closing sale price of $17.51 per share as reported on the NASDAQ Global Select Market on that date was $103,587,847 The registrant has provided this information as of February 28, 2014 because its common stock was not publicly traded as of the last business day of its most recently completed second fiscal quarter. Shares of the registrant s common stock held by each executive officer, director and holder of 5% or more of the outstanding common stock have been excluded in that such persons may be deemed to be affiliates. This calculation does not reflect a determination that certain persons are affiliates of the registrant for any other purpose.

As of February 28, 2014, the registrant had 18,147,544 shares of common stock, par value $0.001, outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

None.

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INOGEN, INC.

PART I

Forward-Looking Statements

This Annual Report on Form 10-K contains forward-looking statements that are based on our management s beliefs and assumptions and on information currently available to our management. The forward-looking statements are contained principally in the sections entitled Business, Risk factors, and Management s discussion and analysis of financial condition and results of operations. Forward-looking statements include information concerning our possible or assumed future results of operations, business strategies, financing plans, competitive position, industry environment, potential growth opportunities, and the effects of competition. Forward-looking statements include statements that are not historical facts and can be identified by terms such as anticipates, believes, could, seeks, estimates, expects, intends, may, plans, potential, predicts, projects, should, will, would, or similar expressions and the negatives of those terms.

Forward-looking statements involve known and unknown risks, uncertainties, and other factors that may cause our actual results, performance, or achievements to be materially different from any future results, performance, or achievements expressed or implied by the forward-looking statements. We discuss these risks in greater detail in the section entitled Risk factors and elsewhere in this Annual Report on Form 10-K. Given these uncertainties, you should not place undue reliance on these forward-looking statements.

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

ITEM 1. BUSINESS

General

We are a medical technology company that 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 we call 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. Our proprietary Inogen One systems concentrate the air around the patient to offer a single source of supplemental oxygen anytime, anywhere with a portable device weighing approximately 4.8 or 7.0 pounds. Our Inogen One G3 and G2 have up to 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. Our systems reduce the patient s reliance on stationary concentrators and scheduled deliveries of tanks with a finite supply of oxygen, thereby improving patient quality of life and fostering mobility.

Although portable oxygen concentrators represent the fastest-growing segment of the Medicare oxygen therapy market, we estimate based on 2012 Medicare data that patients using portable oxygen concentrators represent

approximately 4% to 5% of the total addressable oxygen market in the United States. Based on 2012 industry data, we were 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. We believe we are the only manufacturer of portable oxygen concentrators that employs a direct-to-consumer

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strategy in the United States, meaning we market our products to patients, process their physician paperwork, provide clinical support as needed and bill Medicare or insurance on their behalf. To pursue a direct-to-consumer strategy, our 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.

We believe our direct-to-consumer strategy has been critical to driving patient adoption of our technology. Other portable oxygen concentrator manufacturers access patients by selling through home medical equipment providers that we believe are disincentivized to encourage adoption of portable oxygen concentrators. In order to facilitate the regular delivery and pickup of oxygen tanks, home medical equipment providers have invested in geographically dispersed distribution infrastructure consisting of delivery vehicles, physical locations and delivery personnel within each area. Because portable oxygen concentrators eliminate the need for a physical distribution infrastructure, but have higher initial equipment costs than the delivery model, we believe converting to a portable oxygen concentrator model would require significant restructuring and capital investment for home medical equipment providers. Our direct-to-consumer marketing strategy allows us to sidestep the home medical equipment channel, appeal to patients directly and capture both the manufacturing and provider margin associated with long-term oxygen therapy. We believe our ability to capture this top-to-bottom margin, combined with our portable oxygen concentrators technology that eliminates the need for the service and infrastructure costs associated with the delivery model, gives us a cost structure advantage over our competitors.

Since adopting our direct-to-consumer strategy in 2009 following our acquisition of Comfort Life Medical Supply, LLC, which had an active Medicare billing number but few other assets and limited business activities, we have directly sold or rented our Inogen One systems to more than 40,000 patients, growing our revenue from $10.7 million in 2009 to $75.4 million in 2013. In 2013, 22% of our revenue came from our international markets and 41% of our revenue came from oxygen rentals. Our percentage of rental revenue increased from 35.8% in 2011, increasing our proportion of recurring revenue. Additionally, we have increased our gross margin from 49.3% in 2012 to 51.7% in 2013 primarily due to the change in sales mix toward direct-to-consumer from provider sales, improving system reliability, reducing material cost per system and lowering overhead cost per system. Our net loss was $2.6 million in 2009 transitioning to net income of $25.4 million in 2013. Adjusted net income excluding a one-time tax benefit was $3.6 million in 2013.

Our solution

Our Inogen One systems provide patients who require long-term oxygen therapy with a reliable, lightweight single solution product that improves quality-of-life, fosters mobility and eliminates dependence on both oxygen tanks and cylinders as well as stationary concentrators. We believe our direct-to-consumer strategy increases our ability to effectively develop, design and market our Inogen One solutions, as it allows us to:

- drive patient awareness of our portable oxygen concentrator through direct marketing, sidestepping the home medical equipment channel that other manufacturers rely upon across their homecare businesses, and that is incentivized to continue to service oxygen patients through the delivery model;

- capture the manufacturer and home medical equipment provider margins, allowing us to focus on the total cost of the solution and to invest in the development of product features instead of being constrained by the price required to attract representation from a distribution channel. For example, we have invested in features

that improve patient satisfaction, product durability, reliability and longevity, which increase the cost of our hardware, but reduce the total cost of our solution by reducing our maintenance and repair cost; and

access and utilize direct patient feedback in our research and development efforts, allowing us to innovate based on this feedback and stay at the forefront of patient preference. For example, we have integrated a double battery into our product offering based on direct patient feedback.

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We believe the combination of our direct-to-consumer strategy with our singular focus on designing and developing oxygen concentrator technology has created the best-in-class portfolio of portable oxygen concentrators. Our two current product offerings, the Inogen One G3 and Inogen One G2, at approximately 4.8 and 7.0 pounds, respectively, are amongst the most lightweight portable oxygen concentrators on the market. We believe our Inogen One solutions offer the following benefits:

Single solution for home, ambulatory, travel and nocturnal treatment. We believe our Inogen One solutions are the only portable oxygen concentrators marketed as a single solution, by which we mean a patient can use our Inogen One systems as their only supplemental oxygen source with no need to also use a stationary concentrator regularly. Our compressors are specifically designed to enable our patients to run our portable oxygen concentrators 24/7, whether powered by battery or plugged into an outlet at home or in a car while the battery is recharging.

Reliability. We have made product performance a priority and have improved reliability with each generation. For example, we have introduced patented air-dryer and patent-pending user-replaceable sieve beds to our products, which have improved product performance and, as a result, patient satisfaction. Reliability is not only critical to patient satisfaction, but also cost management, as our minimal physical infrastructure makes product exchanges more costly to us than providers with greater local physical infrastructure.

Effective for nocturnal use. Our Intelligent Delivery Technology enables our portable oxygen concentrators to provide consistent levels of oxygen during sleep despite decreased respiratory rates. As a result, patients can rely on the Inogen One G3 and Inogen One G2 portable oxygen concentrators overnight while sleeping.

Unparalleled flow capacity. Our 4.8 pound Inogen One G3 has at least 50% more flow capacity than other sub-5 pound portable oxygen concentrators, and our 7.0 pound Inogen One G2 has at least 15% more flow capacity than other sub-10 pound portable oxygen concentrators.

User friendly features. Our systems are designed with multiple user friendly features, including long battery life and low noise-levels in their respective weight categories.

Our Inogen One systems

We market our current product offerings, the Inogen One G3 and the Inogen One G2, as single solutions for oxygen therapy. This means our solutions can operate on a 24/7 basis for at least 60 months without a stationary concentrator. We believe the technology in our Inogen One G3 and our Inogen One G2 is effective for nocturnal use. Our Inogen One G2 and the Inogen One G3 are sub-5 and sub-10 pound portable oxygen concentrators that can operate reliably and cost-effectively over the long period of time needed to service oxygen therapy patients without supplemental use of a stationary concentrator or a replacement portable oxygen concentrator. To the extent our competitors portable oxygen solutions require supplemental use of a stationary oxygen concentrator, their solutions are less cost-effective and less convenient for patients. The following table summarizes our key product features:

Key Product Specifications

	Inogen One G3	Inogen One G2
Capacity (ml/min)	840	1,260
Weight (lbs)	4.8 (single battery) 5.8 (double battery)	7.0 (single battery) 8.4 (double battery)
Battery run-time	Up to 4.5 hours (single battery) Up to 9.0 hours (double battery)	Up to 5 hours (single battery) Up to 10 hours (double battery)
Maintenance prevention advantages	User replaceable oxygen filtration cartridges & battery	Air dryer & user replaceable battery
Technology effective for overnight use	Yes	Yes
Sound	42 dBA	38 dBA

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We have focused our research and development efforts on creating solutions that we believe have overcome the reputation of portable oxygen concentrators as being limited in durability and reliability as well as unsuitable for nighttime or 24/7 use. We specifically designed our compressors for 24/7 use. We have worked to improve our reliability and reduce service costs by equipping our portable oxygen concentrators with features such as membrane air dryers and user replaceable filtration cartridges.

All of our Inogen One systems are equipped with Intelligent Delivery Technology, a form of pulse-dose technology from which the patient receives a bolus of oxygen upon inhalation. Pulse dose technology was developed to extend the number of hours an oxygen tank would last and is generally used on all ambulatory oxygen therapy devices. Our proprietary conserver technology utilizes differentiated triggering sensitivity to quickly detect a breath and ensure oxygen delivery within the first 400 milliseconds of inspiration, the interval when oxygen has the most effect on lung gas exchange. During periods of sleep, respiratory rates typically decrease. Our Inogen One systems actively respond to this changing physiology through the use of proprietary technology that increases bolus size. Our Intelligent Delivery Technology is designed to provide effective levels of blood oxygen saturation during sleep and all other periods of rest and activity that are substantially equivalent to continuous flow systems.

The Inogen One G3, our next-generation product, is among the most lightweight products on the market with substantially higher oxygen production capabilities than the other sub-5 pound portable oxygen concentrators on the market. We believe the performance parameters around the Inogen One G3 and Inogen One G2 allow us to serve approximately 95% of the ambulatory oxygen patients and enable us to address a patient s particular clinical needs, as well as lifestyle and performance preferences.

Our direct-to-consumer business model has enabled us to receive direct patient feedback, and we have used this feedback to create portable oxygen concentrators that address the full suite of features and benefits critical to patient preference and retention. Our products prevent patients from having to choose between lightweight size, suitability for 24/7 use, reliability, and key features such as battery life, flow and reduced noise levels.

Sales and marketing

Our direct-to-consumer sales and marketing efforts are focused on generating awareness and demand for our Inogen One systems among patients, physicians and other clinicians, and third-party payors. In the United States as of December 31, 2013 we employed a marketing team of 5 people, an in-house sales team of 120 people, and a field-based sales force of 15 people. Of the $59 million of our 2013 revenue derived from the United States, approximately 52% represented direct-to-patient rentals, 30% represented cash pay sales to patients and 18% represented sales to third-party home medical equipment providers.

Our Medicare and private insurance patients rent our systems, while a portion of our patients choose to purchase our Inogen One products directly. Our ability to rent to patients directly, bill third-party payors on their behalf, and service patients in their homes requires that we hold a valid Medicare supplier number, are accredited by an independent agency approved by Medicare, and comply with the unique licensure and process requirements in the 49 states in which we serve patients.

We use a variety of direct-to-consumer marketing strategies to generate interest in our solutions among current oxygen therapy patients. After a patient contacts us, we guide them through product selection and insurance eligibility, and, if they choose to move forward, process the necessary reimbursement and physician paperwork on their behalf, as well as coordinate the shipping, instruction, and clinical setup process. In accordance with Medicare regulations we do not initially contact patients directly and contact them only upon an inbound inquiry. The below chart describes our United States direct-to-consumer sales process.

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In addition to the direct-to-consumer sales model, we are increasingly utilizing a physician referral model as a complementary sales method. Under this model, our field sales representatives work with physicians in the representative s territory to help physicians understand our products and the value these products provide for patients. We believe that by educating physicians on our products, we can cost-effectively supplement our direct-to-consumer sales and capture a greater number of patients earlier in the course of their oxygen therapy.

We engage in a number of other initiatives to increase awareness, demand, and orders for Inogen One systems. These include attendance at oxygen therapy support groups, guest speaking arrangements at trade shows, and product demonstrations as requested. Additionally, we are targeting private payors to become an in-network provider of oxygen therapy solutions, which we expect will reduce or eliminate any additional patient co-insurance associated with using our solution. We believe this will result in both increased conversion of our initial leads, as well as direct referrals from insurance companies in some cases.

International

Approximately 22% of our sales were from outside the United States in 2013. We sell our products in 43 countries outside the United States through distributors or directly to large house accounts, which include gas companies and home oxygen providers. In this case, we sell to and bill the distributor or house accounts directly, leaving the patient billing, support, and clinical setup to the local provider. As of December 31, 2013, we had four people who focused on selling our products to distributors and house accounts worldwide. In fiscal year 2012, an international distributor accounted for 12% of our revenue. However, no single customer represented more than 10% of our total revenue for 2013.

International sales have been a rapidly growing portion of our business, and we estimate there are 2 million long-term oxygen therapy patients outside of the United States. We believe that the international market is attractive for the following reasons:

- More favorable reimbursement in certain countries, including France and the United Kingdom, where portable oxygen concentrators receive more favorable reimbursement than in the United States.

- Less developed oxygen delivery infrastructure in some countries. We believe that some countries outside the United States have less developed oxygen delivery infrastructure than in the United States. As a result, portable oxygen concentrators enable providers to reach and service patients they cannot economically reach with the delivery model.

- An absence of reimbursement for any ambulatory oxygen therapy modalities in some countries, resulting in patients bearing all of the cost of ambulatory oxygen therapy and therefore becoming more involved in the selection of the modality. In Australia, for example, patients shoulder the burden of all costs associated with ambulatory oxygen therapy. In these cases, they tend to choose products like portable oxygen concentrators that provide a higher level of personal freedom.

We will continue to focus on building out our international sales efforts.

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Customer support and order fulfillment

Our procedures enable us to package and ship a system directly to the patient in the patient s preferred configuration the same day the order is received. This enables us to minimize the amount of finished goods inventory we keep on hand. Our primary logistics partner is United Parcel Service, or UPS. UPS supports both our domestic and international shipments and provides additional services that support our direct-to-consumer oxygen therapy program. The UPS pick up service is used to retrieve patient paperwork, products requiring repair and systems that are no longer needed by the patient. Additionally, UPS, when necessary and requested by us, will go into a patient s home to remove a replacement product from the box, box the failed device and return it to us. In this manner, we are able to operate as a remote provider while maintaining the level of customer service of a local oxygen therapy provider.

We believe it is crucial to provide patients with the highest quality customer support to achieve satisfaction with our products and optimal outcomes. As of December 31, 2013, we had a dedicated client service team of 24 people who were trained on our products, a clinical support team of 16 people who were licensed nurses or respiratory therapists, and a dedicated billing services team of 50 people. We provide our patients with a dedicated 24/7 hotline that is only given to our Inogen One patients and is not published publicly. Via the hotline, patients have direct access to our client services representatives, who can handle product-related questions. Additionally, clinical staff is on call 24/7 and available to patients whenever either the patient or the client services representative deems appropriate. Our dedicated billing services team is available to answer patient questions regarding invoicing, reimbursement, and account status during normal business hours. We receive no additional reimbursement for patient support, but provide high-quality customer service to enhance patient comfort, satisfaction, compliance, and safety with our products. We believe our focus on providing the highest level of customer service has helped drive our sustained patient satisfaction rating of approximately 95%.

Third-party reimbursement

Medicare or private insurance rentals represented approximately 41% of our revenue in 2013. In cases where we rent our oxygen therapy solutions directly to patients, we bill third-party payors, such as Medicare or private insurance, for monthly rentals on behalf of our patients. We process and coordinate all physician paperwork necessary for reimbursement of our solutions. A common medical criterion for oxygen therapy reimbursement is insufficient blood oxygen saturation level. Our team in sales and sales administration are trained on how to verify benefits, review medical records and process physician paperwork. Additionally, an independent internal review is performed and our products are not deployed until after physician paperwork is processed and reimbursement eligibility is verified and communicated to the patient. As of December 31, 2013, our sales and sales administration consisted of 135 people.

We are authorized by Medicare to bill for oxygen therapy, and we believe that more than 60% of oxygen therapy patients have Medicare coverage. Our Inogen One systems are reimbursed under HCPCS codes E1390 and E1392. E1390 covers stationary/nocturnal oxygen therapy systems, while E1392 provides additional reimbursement for portable oxygen concentrators for the treatment of ambulatory patients. Even though E1390 is a stationary oxygen code, we bill under both the E1390 and E1392 codes for our portable oxygen concentrators, assuming that the patient qualifies for portable oxygen, as well as stationary oxygen. Only in the event the patient solely qualifies for portable oxygen would we exclusively bill under the E1392 code, which is not typical. Currently, Medicare reimburses oxygen therapy as a monthly rental for up to 36 months. We retain equipment ownership at all times. After 36 months, payment is capped, meaning the monthly payment amounts are discontinued. After five years or another qualifying event, the patient is eligible for replacement equipment and a new capped rental period.

As of January 1, 2011, Medicare has phased in a program called competitive bidding. Competitive bidding impacts the amount Medicare pays suppliers for durable medical equipment, including portable oxygen concentrators. The

program is defined geographically, with suppliers submitting bids to provide medical equipment for a specific product category within that geography. Once bids have been placed, an individual

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company s bids across products within the category are aggregated and weighted by each product s market share in the category. The weighted average price is then indexed against competitors. Medicare determines a clearing price out of these weighted average prices at which sufficient suppliers have indicated they will support patients in the category, and this threshold is typically designed to have theoretical supply two times greater than expected demand. Bids for each modality among the suppliers that made the cut are then arrayed to determine what Medicare will reimburse for each product category. The program has strict anti-collusion guidelines to ensure bidding is truly competitive. Competitive bidding contracts last three years once implemented, after which they are subject to re-bidding or competitive bidding re-compete.

The competitive bidding program effectively reduces the number of oxygen suppliers that can participate in the Medicare program. We believe that more than 75% of existing oxygen suppliers were eliminated in round one of competitive bidding implemented January 1, 2011 in 9 U.S. Metropolitan Statistical Areas. Round two of competitive bidding was implemented July 1, 2013 in 91 U.S. Metropolitan Statistical Areas and we believe the impact on the number of oxygen suppliers will be similar when released. Combined with the round one of competitive bidding, we believe that approximately 59% of the market was covered by round one and two. The following table sets forth the current standard Medicare reimbursement rates and the weighted average of reimbursement rates applicable in Metropolitan Statistical Areas covered by rounds one and two of competitive bidding. The round one re-compete was completed in the same Metropolitan Statistical Areas as round one for the next three year period starting January 1, 2014 when the original contracts expire.

	Medicare standard allowable effective 1/1/14	**Round one weighted average 1/1/11-12/11/13**	**Round two weighted average 7/1/13-6/30/16**	**Round one recompete weighted average 1/1/14-12/31/16**
E1390	$ 178.24	$ 116.16	$ 93.07	$ 95.74
E1392	51.63	41.89	42.72	38.08
Total	$ 229.87	$ 158.05	$ 135.79	$ 133.82
% of standard		69%	59%	58%

Medicare has not announced specific plans to implement competitive bidding nationwide, but by 2016 Medicare must implement competitive bidding or competitive bidding pricing for included items in non-competitive bidding areas. In February 2014, Medicare solicited public comment on the methodology it would use to comply with this statute.

As of December 31, 2013, we had contracts with 44 non-Medicare payors. These contracts enable us to become an in-network provider for these payors, which enables patients to use our systems at the same cost as other in-network solutions, including the delivery model. Based on our patient population, we believe non-Medicare payors represent at least 30% of all oxygen therapy patients. We believe that private payor reimbursement levels will generally be reset in accordance with Medicare reimbursement level determined by competitive bidding.

We cannot predict the extent to which reimbursement for our products will be affected by competitive bidding or by initiatives to reduce costs for private payors. The unavailability of third-party coverage or inadequacy of reimbursement for our current or future products would adversely affect our business, financial conditions, and results of operations.

Manufacturing

We have been developing and refining the manufacturing of our Inogen One systems over the past eight years. While nearly all of our manufacturing and assembly process was originally outsourced, assembly of the manifold, compressor, sieve bed and concentrator is now conducted in-house in order to improve quality control

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and reduce cost. Additionally, we use lean manufacturing practices to maximize our manufacturing efficiency. Bringing manufacturing and assembly largely in-house, combined with our consistent focus on driving efficient manufacturing processes, has enabled us to reduce our cost of revenue per system by 40% over the past four years.

We rely on third party manufacturers to supply several components of our Inogen One systems. We typically enter into supply agreements for these components that specify quantity, quality requirements, and delivery terms, which, in certain cases, can be terminated by either party upon relatively short notice. We have elected to source certain key components from single sources of supply, including our batteries, bearings, carry bags, motors, pistons, valves, and molded plastic components. While alternative sources of supply are readily available for these components, we believe that maintaining a single-source of supply allows us to control production costs and inventory levels, and to manage component quality. In order to mitigate against the risks related to a single-source of supply, we qualify alternative suppliers and develop contingency plans for responding to disruptions. If any single-source supplier were no longer able to supply a component, we believe we would be able to promptly and cost-effectively switch to an alternative supplier without a significant disruption to our business and operations. We have adopted additional contingency plans to protect against an immediate disruption in supply of our battery and motor components, and any potential delay that may result from a switch to a new supplier. These contingency plans include our own inventory management, along with a requirement that each supplier maintains specified quantities of inventory in multiple locations, and our maintenance of back-up tooling that can easily be transferred to the new supplier. We believe that these contingency plans would limit any disruption to our business in the event of an immediate termination of either our battery or motor supply.

We currently manufacture in two leased buildings in Goleta, California and Richardson, Texas, which we have registered with the FDA and for which have obtained ISO 13485 certification. The Goleta, California facility is approximately 39,000 square feet. The Richardson, Texas facility is approximately 31,000 square feet. Because we have two separate manufacturing facilities, in the event one facility is incapacitated, the other facility will enable us to continue manufacturing our products to meet our current level of demand. We believe we have sufficient capacity to meet anticipated demand.

Our entire organization is responsible for quality management. Our Quality Assurance department oversees this by tracking component, device and organization performance and by training team members outside the Quality Assurance department to become competent users of our Quality Management system. By measuring component performance, communicating daily with the production group and our suppliers, and reviewing customer complaints, our Quality Assurance department, through the use of our corrective action program, drives and documents continuous performance improvement of our suppliers and internal departments. Our Quality Assurance department also trains internal auditors to audit our adherence to the Quality Management system. Our Quality Management system has been certified to International Standards Organization, or ISO, 13485:2012 by Intertek, a Notified Body to ISO.

As a medical device manufacturer, our manufacturing facilities are subject to periodic inspection by the FDA and certain corresponding state agencies. We have been audited twice since April 2012 by the FDA and found to be in compliance with Good Manufacturing Practices guidelines. We have completed two surveillance audits by our notifying body over the same period and identified one minor non-conformance, which is currently being addressed through implementation of new training software. Additionally, we have had two unannounced inspections by state inspectors from California and Texas within the past year and were determined to be in complete compliance with state health and safety requirements.

As of December 31, 2013, we had approximately 76 employees in operations, manufacturing and quality assurance.

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Research and development

We are committed to ongoing research and development to stay at the forefront of patient preference in the oxygen concentrator field. As of December 31, 2013, our research and development staff included 16 engineers and scientists with expertise in air separation, compressors, pneumatics, electronics, embedded software, mechanical design, sensors and manufacturing technologies. Our current research and development efforts are focused primarily on increasing functionality, improving design for ease-of-use, and reducing production costs of our Inogen One systems, as well as development of our next-generation oxygen concentrators. Over the last 3 fiscal years, Inogen has invested over $6.5 million to efficiently bring two new generations of portable oxygen concentrators to market ($2.4, $2.3 and $1.8 million for the years ended 2013, 2012 and 2011), leveraging our 24 issued U.S. patents and one issued Canadian patent while also reducing the bill of product costs 36% from the original Inogen One G1.

Utilizing lean product development methodologies, we have released three generations of disruptive products over the last 10 years into the marketplace, including our Inogen One G1 in October 2004, our Inogen One G2 in March 2010, and our Inogen One G3 in September 2012. Our dedication to continuous improvement has also resulted in three mid-cycle product updates and numerous incremental improvements. Development projects utilize a combination of rapid prototyping and accelerated life testing methods to ensure products are taken from concept to commercialization in a fast and capital efficient manner. We leverage our direct patient expertise to rapidly gain insight from end users and to identify areas of innovation that lead to higher-quality products and lower total cost of ownership for its products.

Our product pipeline consists of both a stationary concentrator and a fourth generation, ultra-lightweight portable oxygen concentrators. The stationary concentrator, which we are calling Inogen At Home, will allow us to access non-ambulatory patients and will serve as a backup to our Inogen One patients. We currently provide a backup source of oxygen to our patients who are able to elect either a stationary concentrator or oxygen tank as their backup source. We are not able to bill or be reimbursed for these backup sources and we supply them at our own cost, which is included in our cost of rental revenues. These backup sources are currently acquired from third parties; however, upon the launch of our Inogen At Home product, we will be manufacturing and supplying these stationary backup sources. The Inogen At Home 510(k) submission was received by the FDA s Devices and Radiological Health Document Control Center on August 8, 2013 and is currently in process. We expect to commercialize Inogen At Home in 2014. Our fourth-generation portable oxygen concentrators will be smaller and lighter than our Inogen One G3 and we expect to commercialize this product in the next several years. Additionally, we continue to focus our efforts on other design and functionality improvements that enhance patient quality of life.

Competition

The oxygen therapy market is a highly competitive industry. We compete with a number of manufacturers and distributors of portable oxygen concentrators, as well as providers of other oxygen therapy solutions such as home delivery of oxygen tanks, or cylinders.

Our significant manufacturing competitors are Invacare Corporation, Respironics (a subsidiary of Koninklijke Philips N.V.), AirSep Corporation and SeQual Technologies (subsidiaries of Chart Industries, Inc.), Inova Labs, Inc. and DeVilbiss Healthcare. Given the relatively low barriers to entry in the oxygen therapy device manufacturing market, we expect that the industry will become increasingly competitive in the future. Manufacturing companies compete for sales to providers primarily on the basis of product features, service and price. We believe our manufacturing competitors complete reliance on home medical equipment distribution compresses their margins and limits their ability to invest in product features that address consumer preferences. To pursue a direct-to-consumer strategy, our manufacturing competitors would need to meet national accreditation and state-by-state licensing requirements and

secure Medicare billing privileges, as well as compete directly with the home medical equipment providers that many rely on across their entire homecare businesses. For our two largest medical device competitors, their entire oxygen business, including stationary and homefill, represents less than 13% percent of their billion-dollar plus homecare businesses.

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Lincare Inc., Apria Healthcare, Inc. Rotech Healthcare, Inc. and American HomePatient, Inc. have been among the market leaders in providing oxygen therapy for many years, while the remaining oxygen therapy market is serviced by local providers. Because many oxygen therapy providers were either excluded from contracts in the Medicare competitive bidding process, or will have difficulty providing service at the prevailing Medicare reimbursement rates, we expect more industry consolidation. Oxygen therapy providers compete primarily on the basis of product features and service, rather than price, since reimbursement levels are established by Medicare and Medicaid, or by the individual determinations of private payors. We believe that the investment made by oxygen therapy providers in the physical distribution required for oxygen delivery limits their ability to easily switch their business model and employ a solution directly competitive to Inogen.

Some of our competitors are large, well-capitalized companies with greater resources than we have. As a consequence, they are able to spend more aggressively on product development, marketing, sales and other product initiatives than we can. Some of these competitors have:

- significantly greater name recognition;
- established relations with healthcare professionals, customers and third-party payors;
- established distribution networks;
- additional lines of products, and the ability to offer rebates or bundle products to offer higher discounts or other incentives to gain a competitive advantage;
- greater history in conducting research and development, manufacturing, marketing and obtaining regulatory approval for oxygen device products; and
- greater financial and human resources for product development, sales and marketing, patent litigation and customer financing.

As a result, our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standards or customer requirements. In light of these advantages that our competitors maintain, even if our technology and direct-to-consumer distribution strategy is more effective than the technology and distribution strategy of our competitors, current or potential customers might accept competitor products and services in lieu of purchasing our products. We anticipate that we will face increased competition in the future as existing companies and competitors develop new or improved products and distribution strategies and as new companies enter the market with new technologies and distribution strategies. We may not be able to compete effectively against these organizations. Our ability to compete successfully and to increase our market share is dependent upon our reputation for providing responsive, professional and high-quality products and services and achieving strong customer satisfaction. Increased competition in the future could adversely affect our revenue, revenue growth rate, if any, margins and market share.

Government regulation

Inogen One systems are medical devices subject to extensive and ongoing regulation by the FDA, as well as other federal and state regulatory bodies in the United States and comparable authorities in other countries. The FDA regulations govern the following activities that we perform, or that are performed on our behalf, to ensure that medical products distributed domestically or exported internationally are safe and effective for their intended uses: product design and development, pre-clinical and clinical testing, manufacturing, labeling, storage, pre-market clearance or approval, record keeping, product marketing, advertising and promotion, sales and distribution, and post-marketing surveillance.

FDA s pre-market clearance and approval requirements

Unless an exemption applies, each medical device we seek to commercially distribute in the United States will require either a prior 510(k) clearance or a pre-market approval from the FDA. Medical devices are classified into one of three classes Class I, Class II or Class III depending on the degree of risk associated

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with each medical device and the extent of control needed to ensure safety and effectiveness. Devices deemed to pose lower risks are placed in either Class I or II, which requires the manufacturer to submit to the FDA a premarket notification requesting permission to commercially distribute the device. This process is generally known as 510(k) clearance. Some low risk devices are exempted from this requirement. Devices deemed by the FDA to pose the greatest risk, such as life-sustaining, life-supporting or implantable devices, or devices deemed not substantially equivalent to a previously cleared 510(k) device, are placed in Class III, requiring premarket approval.

510(k) clearance pathway

When a 510(k) clearance is required, we must submit a premarket notification to the FDA demonstrating that our proposed device is substantially equivalent to a previously cleared and legally marketed 510(k) device or a device that was in commercial distribution before May 28, 1976 for which the FDA has not yet called for the submission of a pre-market approval application. By regulation, the FDA is required to clear or deny a 510(k) premarket notification within 90 days of submission of the application. As a practical matter, clearance often takes significantly longer. The FDA may require further information, including clinical data, to make a determination regarding substantial equivalence. If the FDA determines that the device, or its intended use, is not substantially equivalent to a previously-cleared device or use, the FDA will place the device, or the particular use, into Class III. We obtained 510(k) clearance for the original Inogen One system on May 13, 2004. We market the Inogen One G2 and G3 systems pursuant to the original Inogen One 510(k) clearance.

Pre-market approval pathway

A pre-market approval application must be submitted to the FDA if the device cannot be cleared through the 510(k) process. The pre-market approval application process is much more demanding than the 510(k) premarket notification process. A pre-market approval application must be supported by extensive data, including but not limited to technical, preclinical, clinical trials, manufacturing and labeling to demonstrate to the FDA s satisfaction reasonable evidence of safety and effectiveness of the device.

After a pre-market approval application is submitted and the FDA determines that the application is sufficiently complete to permit a substantive review, the FDA will accept the application for review. The FDA has 180 days to review an accepted pre-market approval application, although the review of an application generally occurs over a significantly longer period of time and can take up to several years. During this review period, the FDA may request additional information or clarification of the information already provided. Also, an advisory panel of experts from outside the FDA may be convened to review and evaluate the application and provide recommendations to the FDA as to the approvability of the device. In addition, the FDA will conduct a preapproval inspection of the manufacturing facility to ensure compliance with quality system regulations.

Clinical trials

Clinical trials are almost always required to support pre-market approval and are sometimes required for 510(k) clearance. In the United States, these trials generally require submission of an application for an Investigational Device Exemption, or IDE, to the FDA. The IDE application must be supported by appropriate data, such as animal and laboratory testing results, showing it is safe to test the device in humans and that the testing protocol is scientifically sound. The IDE must be approved in advance by the FDA for a specific number of patients unless the product is deemed a non-significant risk device eligible for more abbreviated IDE requirements. Clinical trials for significant risk devices may not begin until the IDE application is approved by the FDA and the appropriate institutional review boards, or IRBs, at the clinical trial sites. We, the FDA or the IRB at each site at which a clinical trial is being performed may suspend a clinical trial at any time for various reasons, including a belief that the risks to

study subjects outweigh the benefits. Even if a trial is completed, the results of clinical testing may not demonstrate the safety and efficacy of the device, may be equivocal or may otherwise not be sufficient to obtain approval or clearance of the product.

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Pervasive and ongoing regulation by the FDA

Even after a device receives clearance or approval and is placed on the market, numerous regulatory requirements apply. These include:

- establishment registration and device listing;
- quality system regulation, which requires manufacturers, including third-party manufacturers, to follow stringent design, testing, control, documentation and other quality assurance procedures during all aspects of the manufacturing process;
- labeling regulations and the FDA prohibitions against the promotion of products for un-cleared, unapproved or off-label uses, and other requirements related to promotional activities;
- medical device reporting regulations, which require that manufacturers report to the FDA if their device may have caused or contributed to a death or serious injury or malfunctioned in a way that would likely cause or contribute to a death or serious injury if the malfunction were to recur;
- corrections and removals reporting regulations, which require that manufacturers report to the FDA field corrections and product recalls or removals if undertaken to reduce a risk to health posed by the device or to remedy a violation of the Federal Food, Drug and Cosmetic Act that may present a risk to health; and
- post-market surveillance regulations, which apply when necessary to protect the public health or to provide additional safety and effectiveness data for the device.

After a device receives 510(k) clearance or a pre-market approval, any modification that could significantly affect its safety or effectiveness, or that would constitute a major change in its intended use, will require a new clearance or approval. The FDA requires each manufacturer to make this determination initially, but the FDA can review any such decision and can disagree with a manufacturer s determination. We have modified various aspects of our Inogen One systems since receiving regulatory clearance, but we believe that new 510(k) clearances are not required for these modifications. If the FDA disagrees with our determination not to seek a new 510(k) clearance, the FDA may retroactively require us to seek 510(k) clearance or pre-market approval. The FDA could also require us to cease marketing and distribution and/or recall the modified device until 510(k) clearance or pre-market approval is obtained. Also, in these circumstances, we may be subject to significant regulatory fines and penalties.

Failure to comply with applicable regulatory requirements can result in enforcement action by the FDA, which may include any of the following sanctions: Warning Letters, fines, injunctions, civil or criminal penalties, recall or seizure of our products, operating restrictions, partial suspension or total shutdown of production, refusing our request for 510(k) clearance or pre-market approval of new products, rescinding previously granted 510(k) clearances or withdrawing previously granted pre-market approvals.

We are subject to announced and unannounced inspections by the FDA, and these inspections may include the manufacturing facilities of our subcontractors. Inogen has been audited twice since April 2012 by the FDA and found to be in compliance with the Quality System Regulation. We cannot assure you that we can maintain a comparable level of regulatory compliance in the future at our facility.

International sales of medical devices are subject to foreign government regulations, which may vary substantially from country to country. The time required to obtain approval by a foreign country may be longer or shorter than that required for FDA approval, and the requirements may differ. There is a trend towards harmonization of quality system standards among the European Union, United States, Canada and various other industrialized countries.

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Licensure

In April 2009, we became a Durable, Medical Equipment, Prosthetics, Orthotics, and Supplies accredited Medicare supplier by Accreditation Commission for Health Care for our Goleta, California facility for Home/Durable Medical Equipment Services for oxygen equipment and supplies. Our Medicare accreditation must be renewed every three years through passage of an on-site inspection. Our current accreditation with Medicare is due to expire in May 2015. Several states require that durable medical equipment providers be licensed in order to sell products to patients in that state. Certain of these states require that durable medical equipment providers maintain an in-state location. Most of our state licenses are renewed on an annual or bi-annual basis. Although we believe we are in compliance with all applicable state regulations regarding licensure requirements, if we were found to be noncompliant, we could lose our licensure in that state, which could prohibit us from selling our current or future products to patients in that state. In addition, we are subject to certain state laws regarding professional licensure. We believe that our certified clinicians are in compliance with all such state laws. If our clinicians were to be found non-compliant in a given state, we would need to modify our approach to providing education, clinical support and customer service in such state.

Federal anti-kickback and self-referral laws

The Federal Anti-Kickback Statute prohibits the knowing and willful offer, payment, solicitation or receipt of any form of remuneration in return for, or to induce the:

- referral of a person;
- furnishing or arranging for the furnishing of items or services reimbursable under Medicare, Medicaid or other governmental programs; or
- purchase, lease, or order of, or the arrangement or recommendation of the purchasing, leasing, or ordering of any item or service reimbursable under Medicare, Medicaid or other governmental programs.

The Federal Anti-Kickback Statute applies to our arrangements with sales representatives, customers and health care providers, as well as certain coding and billing information that we may provide to purchasers of Inogen One systems. Although we believe that we have structured such arrangements to be in compliance with the Anti-Kickback Statute and other applicable laws, regulatory authorities may determine otherwise. Noncompliance with the federal anti-kickback statute can result in exclusion from Medicare, Medicaid or other governmental programs, restrictions on our ability to operate in certain jurisdictions, as well as civil and criminal penalties, any of which could have an adverse effect on our business and results of operations.

Federal law also includes a provision commonly known as the Stark Law, which prohibits a physician from referring Medicare or Medicaid patients to an entity providing designated health services, including a company that furnishes durable medical equipment, in which the physician has an ownership or investment interest or with which the physician has entered into a compensation arrangement. Violation of the Stark Law could result in denial of payment, disgorgement of reimbursements received under a noncompliant arrangement, civil penalties, and exclusion from Medicare, Medicaid or other governmental programs. Although we believe that we have structured our provider arrangements to comply with current Stark Law requirements, these arrangements may not expressly meet the requirements for applicable exceptions from the law.

Additionally, as some of these laws are still evolving, we lack definitive guidance as to the application of certain key aspects of these laws as they relate to our arrangements with providers with respect to patient training. We cannot predict the final form that these regulations will take or the effect that the final regulations will have on us. As a result, our provider arrangements may ultimately be found to be not in compliance with applicable federal law.

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Federal false claims act

The Federal False Claims Act provides, in part, that the federal government may bring a lawsuit against any person whom it believes has knowingly presented, or caused to be presented, a false or fraudulent request for payment from the federal government, or who has made a false statement or used a false record to get a claim approved. In addition, amendments in 1986 to the Federal False Claims Act have made it easier for private parties to bring qui tam whistleblower lawsuits against companies. Although we believe that we are in compliance with the federal government s laws and regulations, if we are found in violation of these laws, penalties include fines ranging from $5,500 to $11,000 for each false claim, plus three times the amount of damages that the federal government sustained because of the act of that person. We believe that we are in compliance with the federal government s laws and regulations concerning the filing of reimbursement claims.

Civil monetary penalties law

The Federal Civil Monetary Penalties Law prohibits the offering or transferring of remuneration to a Medicare or Medicaid beneficiary that the person knows or should know is likely to influence the beneficiary s selection of a particular supplier of Medicare or Medicaid payable items or services. We sometimes offer customers various discounts and other financial incentives in connection with the sales of our products. While it is our intent to comply with all applicable laws, the government may find that our marketing activities violate the Civil Monetary Penalties Law. If we are found to be in noncompliance, we could be subject to civil money penalties of up to $10,000 for each wrongful act, assessment of three times the amount claimed for each item or service and exclusion from the Federal healthcare programs. In addition, to the extent we are found to not be in compliance, we may be required to curtail or restructure our operations. Any penalties, damages, fines, exclusions, curtailment or restructuring of our operations could adversely affect our ability to operate our business and our financial results.

State fraud and abuse provisions

Many states have also adopted some form of anti-kickback and anti-referral laws and false claims act that may apply to all payors. We believe that we are in compliance with such laws. Nevertheless, a determination of liability under such laws could result in fines and penalties and restrictions on our ability to operate in these jurisdictions.

HIPAA

In addition to creating the two new federal healthcare crimes, regulations implementing HIPAA also establish uniform standards governing the conduct of certain electronic healthcare transactions and protecting the security and privacy of individually identifiable health information maintained or transmitted by healthcare providers, health plans and healthcare clearinghouses, which are referred to as covered entities. Three standards have been promulgated under HIPAA s regulations: the Standards for Privacy of Individually Identifiable Health Information, which restrict the use and disclosure of certain individually identifiable health information, the Standards for Electronic Transactions, which establish standards for common healthcare transactions, such as claims information, plan eligibility, payment information and the use of electronic signatures, and the Security Standards, which require covered entities to implement and maintain certain security measures to safeguard certain electronic health information, including the adoption of administrative, physical and technical safeguards to protect such information.

In 2009, Congress passed the American Recovery and Reinvestment Act of 2009, or ARRA, which included sweeping changes to HIPAA, including an expansion of HIPAA s privacy and security standards. ARRA includes HITECH, which, among other things, made HIPAA s privacy and security standards directly applicable to business associates of covered entities effective February 17, 2010. A business associate is a person or entity that performs certain functions

or activities on behalf of a covered entity that involve the use or disclosure of protected health information in connection with recognized health care operations activities. As a result, business

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associates are now subject to significant civil and criminal penalties for failure to comply with applicable standards. Moreover, HITECH creates a new requirement to report certain breaches of unsecured, individually identifiable health information and imposes penalties on entities that fail to do so. HITECH also increased the civil and criminal penalties that may be imposed against covered entities, business associates and possibly other persons and gave state attorneys general new authority to file civil actions for damages or injunctions in federal courts to enforce the federal HIPAA laws and seek attorney fees and costs associated with pursuing federal civil actions. The 2013 final HITECH omnibus rule modifies the breach reporting standard in a manner that will likely make more data security incidents qualify as reportable breaches.

In addition to federal regulations issued under HIPAA, some states have enacted privacy and security statutes or regulations that, in some cases, are more stringent than those issued under HIPAA. In those cases, it may be necessary to modify our planned operations and procedures to comply with the more stringent state laws. If we fail to comply with applicable state laws and regulations, we could be subject to additional sanctions. Any liability from failure to comply with the requirements of HIPAA, HITECH or state privacy and security statutes or regulations could adversely affect our financial condition. The costs of complying with privacy and security related legal and regulatory requirements are burdensome and could have a material adverse effect on our results or operations.

International regulation

International sales of medical devices are subject to foreign governmental regulations, which vary substantially from country to country. The time required to obtain clearance or approval by a foreign country may be longer or shorter than that required for FDA clearance or approval, and the requirements may be different.

The primary regulatory environment in Europe is that of the European Union, which has adopted numerous directives and has promulgated voluntary standards regulating the design, manufacture, clinical trials, labeling and adverse event reporting for medical devices. Devices that comply with the requirements of a relevant directive will be entitled to bear the CE conformity marking, indicating that the device conforms with the essential requirements of the applicable directives and, accordingly, can be commercially distributed throughout the member states of the European Union, and other countries that comply with or mirror these directives. The method of assessing conformity varies depending on the type and class of the product, but normally involves a combination of self-assessment by the manufacturer and a third-party assessment by a notified body, an independent and neutral institution appointed by a country to conduct the conformity assessment. This third-party assessment may consist of an audit of the manufacturer s quality system and specific testing of the manufacturer s device. Such an assessment may be required in order for a manufacturer to commercially distribute the product throughout these countries. ISO 9001 and ISO 13845 certifications are voluntary standards. Compliance establishes the presumption of conformity with the essential requirements for a CE Marking. We have the authorization to affix the CE Mark to our products and to commercialize our devices in the European Union. Our ISO 13485 certification was issued on April 21, 2005 and our EC-Certificate was issued on March 16, 2007.

Before we can sell our devices in Canada we must submit and obtain clearance of a license application, implement and comply with ISO Standard 13485, and undergo an audit by a registrar accredited by Health Canada. On January 25, 2006, we received our Medical Device License in Canada. In Australia, we must appoint an agent sponsor who will interact on our behalf with the Therapeutics Goods Administration (TGA). We must also prepare a technical file and declaration of conformity to essential requirements under Australian law, provide evidence of CE Marking of the device and submit this information via our agent sponsor to the TGA in a Medical Device Application. On June 4, 2007, we received our Certificate for Inclusion of a Medical Device in Australia.

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Intellectual property

We believe that to maintain a competitive advantage, we must develop and preserve the proprietary aspect of our technologies. We rely on a combination of patent, trademark, trade secret and other intellectual property laws, non-disclosure agreements and other measures to protect our proprietary rights. Currently, we require our employees, consultants and advisors to execute non-disclosure agreements in connection with their employment, consulting or advisory relationships with us, where appropriate. We also require our employees, consultants and advisors who we expect to work on our current or future products to agree to disclose and assign to us all inventions conceived during the work day, developed using our property or that relate to our business. Despite any measures taken to protect our intellectual property, unauthorized parties may attempt to copy aspects of our Inogen One systems or to obtain and use information that we regard as proprietary.

Patents

As of December 31, 2013, we had 24 issued U.S. patents, one issued Canadian patent and six additional pending U.S. patent applications. We anticipate it will take several years for the most recent of these U.S. patent applications to result in issued patents, if at all.

Our patent portfolio contains three principal sets of patents and patent applications. The first set relates to the construction and design of specific Inogen products. For example, U.S. Patent Nos. 8,440,004; 8,366,815; 8,377,181; and 8,568,519 are directed to design elements of the Inogen One G2 portable oxygen concentrator. These patents expire in 2031 (without taking into account any patent term adjustments) and may serve to deter competitors from reverse engineering or copying our design elements. This set of patents and patent applications also contains a pending U.S. patent application that relates to the design of the Inogen One G3 portable oxygen concentrator.

The second set of patents and patent applications within our portfolio pertains to operating algorithms and design optimization techniques. U.S. Patent Nos. 7,841,343; 7,585,351; 7,857,894; 8,142,544; and 6,605,136 are directed to optimization of the Pressure Swing Adsorption oxygen generating system and the oxygen conserving technology used across all of our products. These patents expire in 2027, 2026, 2027, 2026 and 2022 respectively (without taking into account any patent term adjustments). These algorithms and optimization techniques are developed to facilitate the design and manufacturing of our products. These patents may prevent competitors from achieving the same levels of optimization as found in our products.

The third set of patents and patent applications includes system component designs that may be incorporated into our products. For example, U.S. Patent No. 8,580,015, which expires in 2027 (without taking into account any patent term adjustments), is directed to product improvements that have been utilized in the Inogen One and Inogen One G2 products. Also within this class of patents are U.S. Patent Nos. 7,686,870 and 7,922,789 that are directed to designs that may be utilized in future Inogen products to improve performance over current product offerings. These patents expire in 2027 and 2023 respectively (without taking into account any patent term adjustments).

Trademarks

We have registered the trademarks Inogen; Inogen One; Inogen One G2; Oxygenation; Live Life in Moments, not Minutes; Never Run Out of Oxygen; Oxygen Therapy on Your Terms; Oxygen. Anytime. Anywhere; Reclaim Your Independence; Intelligent Delivery Technology; and the Inogen design with the United States Patent and Trademark Office. We have applied with the United States Patent and Trademark Office to register the trademark Inogen at Home. We have registered the trademark Inogen in Australia, New Zealand, Canada, Chile, China, South Korea, Mexico, and in Europe (European Community registration). We have registered the trademark Inogen One in

Australia, Canada, Chile, China, South Korea, Mexico, and in Europe (European Community registration). We have registered the trademark Satellite Conserver in Australia, Mexico, Canada, Chile, China, and in South Korea. We have applied for a European Community registration to register the trademark Inogen at Home.

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Legal proceedings

On November 4, 2011, we 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. We 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 alleging patent invalidity, non-infringement and inequitable conduct. We denied the allegations in the Defendant s counterclaims. We have 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.

Facilities and property

We lease approximately 39,000 square feet of manufacturing and office space at our corporate headquarters in Goleta, California under a lease that expires in September 2015, and approximately 31,000 square feet of manufacturing and office space in Richardson, Texas under a lease that expires in December 2019. In addition, we lease office space in Smyrna, Tennessee, and Corinth, Mississippi under leases expiring in August 2014 and May 2014, respectively. We believe that our existing facilities are adequate to meet our business requirements for the near-term and that additional space will be available on commercially reasonable terms, if required.

Employees

As of December 31, 2013, we had 354 full and part-time employees, including 180 in sales, marketing, clinical and client services, 76 in operations, manufacturing and quality assurance, 82 in general administration and 16 in research and development. None of our employees is represented by a collective bargaining agreement. We believe that our employee relations are good.

Corporate and available information

We were incorporated in Delaware in November 2001. Our principal executive offices are located at 326 Bollay Drive, Goleta, California 93117. Our telephone number is (805) 562-0500. Our website address is *www.inogen.com*. We make available on our website, free of charge, our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K, and any amendments to those reports, as soon as reasonably practicable after we electronically file such material with, or furnish it to, the Securities and Exchange Commission, or SEC. Our SEC reports can be accessed through the investor relations page of our website located at http://investor.inogen.com/sec.cfm Additionally, a copy of this Annual Report on Form 10-K is located at the SEC s Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330.

We webcast our earnings calls and certain events we participate in or host with members of the investment community on our investor relations page of our website. Corporate governance information, including our board committee charters, code of ethics, and corporate governance principles, is also available on our investor

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relations page of our website located at http://investor.inogen.com/ The contents of our website are not incorporated by reference into this Annual Report on Form 10-K or in any other report or document we file with the SEC, and any references to our website are intended to be inactive textual references only.

Environmental matters

Our research and development and manufacturing processes involve the controlled use of hazardous materials, including flammables, toxics, and corrosives. Our research and manufacturing operations produce hazardous chemical waste products. We seek to comply with applicable laws regarding the handling and disposal of such materials. Given the small volume of such materials used or generated at our facilities, we do not expect our compliance efforts to have a material effect on our capital expenditures, earnings, and competitive position. However, we cannot eliminate the risk of accidental contamination or discharge and any resultant injury from these materials. We do not currently maintain separate environmental liability coverage and any such contamination or discharge could result in significant cost to us in penalties, damages, and suspension of our operations.

Backlog

We have no material backlog of orders.

Geographic information

During the 2013 and 2012, all of our long-lived assets were located within the United States. Approximately 22% of our 2013 revenue, 27% of our 2012 revenue, and 26% of our 2011 came from international markets. Please see *Note 2* to our audited financial statements included elsewhere in this Annual Report on Form 10-K for additional information related to our U.S. and non-U.S. revenue.

Seasonality

We believe our sales may be impacted by seasonal factors. For example, we typically experience higher sales in the second quarter, as a result of consumers traveling and vacationing during the summer months.

ITEM 1A. RISK FACTORS

This Annual Report on Form 10-K, or Form 10-K, including any information incorporated by reference herein, contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, referred to as the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, referred to as the Exchange Act. In some cases, you can identify forward-looking statements by terms such as anticipates , believes , estimates , expects , intends , may , plans , projects , will , would or the negative of these terms or other comparable terminology. The forward-looking statements contained in this Form 10-K involve known and unknown risks, uncertainties and situations that may cause our or our industry s actual results, level of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these statements. These factors include those listed below in this Item 1A and those discussed elsewhere in this Form 10-K. We encourage investors to review these factors carefully. We may from time to time make additional written and oral forward-looking statements, including statements contained in our filings with the SEC. We do not undertake to update any forward-looking statement that may be made from time to time by or on behalf of us, whether as a result of new information, future events or otherwise, except as required by law.

Before you invest in our securities, you should be aware that our business faces numerous financial and market risks, including those described below, as well as general economic and business risks. The following discussion provides information concerning the material risks and uncertainties that we have identified and

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believe may adversely affect our business, our financial condition and our results of operations. Before you decide whether to invest in our securities, you should carefully consider these risks and uncertainties, together with all of the other information included in this Form 10-K.

Risks related to our business and strategy

A significant majority of our customers have health coverage under the Medicare program, and recently enacted and future changes in the reimbursement rates or payment methodologies under Medicare and other government programs have affected and could continue to materially and adversely affect our business and operating results.

As a provider of oxygen product rentals, we have historically depended heavily on Medicare reimbursement as a result of the higher proportion of elderly persons suffering from chronic respiratory conditions. Medicare Part B, or Supplementary Medical Insurance Benefits, provides coverage to eligible beneficiaries that include items of durable medical equipment for use in the home, such as oxygen equipment and other respiratory devices. We believe that more than 60% of oxygen therapy patients in the United States have primary coverage under Medicare Part B. In 2013 and 2012, we derived approximately 24%, and 27%, respectively, of our revenue from Medicare. There are increasing pressures on Medicare to control health care costs and to reduce or limit reimbursement rates for home medical products.

Legislation, including the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, the Deficit Reduction Act of 2005, the Medicare Improvements for Patients and Providers Act of 2008, and the Patient Protection and Affordable Care Act, contain provisions that directly impact reimbursement for the durable medical equipment products provided by us:

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 significantly reduced reimbursement for inhalation drug therapies beginning in 2005, reduced payment amounts for certain durable medical equipment, including oxygen, beginning in 2005, froze payment amounts for other covered home medical equipment items through 2008, established a competitive bidding program for home medical equipment and implemented quality standards and accreditation requirements for durable medical equipment suppliers.

The Deficit Reduction Act of 2005 limited the total number of continuous rental months for which Medicare will pay for oxygen equipment to 36 months, after which time there is generally no additional reimbursement to the supplier (other than for periodic, in-home maintenance and servicing). The Deficit Reduction Act of 2005 also provided that title of the equipment would transfer to the beneficiary, which was later repealed by the Medicare Improvements for Patients and Providers Act of 2008. For purposes of the rental cap, the Deficit Reduction Act of 2005 provided for a new 36-month rental period that began January 1, 2006 for all oxygen equipment. After the 36th continuous month during which payment is made for the oxygen equipment, the supplier is generally required to continue to furnish the equipment during the period of medical need for the remainder of the useful lifetime of the equipment, provided there are no breaks in service due to medical necessity that exceed 60 days. The reasonable useful lifetime for portable oxygen equipment is 60 months. After 60 months, if the patient requests, the rental cycle starts over and a new 36-month capped rental period begins. There are no limits on the number of 60-month cycles over which a Medicare patient may receive benefits and an oxygen therapy provider may receive reimbursement, so long as such equipment continues to be medically necessary for the patient. We anticipate that the Deficit

Reduction Act of 2005 oxygen payment rules will continue to negatively affect our net revenue on an ongoing basis, as each month additional customers reach the 36-month capped service period, resulting in potentially two or more years without rental income from these customers. We cannot state with certainty the potential impact to revenue associated with patients in the capped rental period.

Medicare Improvements for Patients and Providers Act of 2008 retroactively delayed the implementation of competitive bidding for 18 months from previously established dates and decreased

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the 2009 fee schedule payment amounts by 9.5% for product categories included in competitive bidding. In addition to the 9.5% reduction under Medicare Improvements for Patients and Providers Act of 2008, the Centers for Medicare & Medicaid Services implemented a reduction to the monthly payment amount for stationary oxygen equipment by 2.3% in 2009 and 1.5% in 2010, which reduced the monthly payment rate to $175.79 and $173.17 in 2009 and 2010, respectively. The stationary oxygen payment rate for 2011 and 2012 was increased by 0.1%, 1.6%, and 0.7% in 2011, 2012, and 2013, respectively, thereby increasing the monthly payment rate to $173.31, $176.06, and $177.36 in 2011, 2012, and 2013, respectively. A Joint Select Committee on Deficit Reduction, tasked with recommending a targeted deficit reduction of at least $1.2 trillion for the years 2013 through 2021, was unable to reach required goals, thereby triggering the legislation s automatic reduction to several government programs. This includes aggregate reductions of Medicare payments to providers up to 2% per fiscal year, which went into effect on April 1, 2013. In 2014, the monthly payment rate for stationary oxygen equipment increased to $178.24, a 0.5% increase. The monthly payment rate for non-delivery ambulatory oxygen in the relevant period was flat at $51.63.

The Patient Protection and Affordable Care Act includes, among other things, a deductible excise tax on any entity that manufactures or imports medical devices offered for sale in the United States, with limited exceptions including oxygen products such as ours, which began in 2013; new face-to-face physician encounter requirements for durable medical equipment and home health services; and a requirement that by 2016, the competitive bidding process must be nationalized or prices in non-competitive bidding areas must be adjusted to match competitive bidding prices.

These legislative provisions, as currently in effect and when fully implemented, have had and will continue to have a material and adverse effect on our business, financial condition and operating results.

Due to budgetary shortfalls, many states are considering, or have enacted, cuts to their Medicaid programs. These cuts have included, or may include, elimination or reduction of coverage for our products, amounts eligible for payment under co-insurance arrangements, or payment rates for covered items. Continued state budgetary pressures could lead to further reductions in funding for the reimbursement for our products which, in turn, would adversely affect our business, financial conditions, and results of operations.

The implementation of the competitive bidding process under Medicare could negatively affect our business and financial condition.

The Medicare Prescription Drug, Improvement, and Modernization Act of 2003 required the Secretary of Health and Human Services to establish and implement programs under which competitive acquisition areas are established throughout the United States for purposes of awarding contracts for the furnishing of competitively priced items of durable medical equipment, including oxygen equipment.

The Centers for Medicare & Medicaid Services, the agency responsible for administering the Medicare program, conducts a competition for each competitive acquisition area under which providers submit bids to supply certain covered items of durable medical equipment. Successful bidders must meet certain program quality standards in order to be awarded a contract and only successful bidders can supply the covered items to Medicare beneficiaries in the acquisition area. There are, however, regulations in place that allow non-contracted providers to continue to provide products and services to their existing customers at the new competitive bidding payment amounts. The contracts are expected to be re-bid every three years. The Centers for Medicare & Medicaid Services is required to award contracts to multiple entities submitting bids in each area for an item or service, but has the authority to limit the number of contractors in a competitive acquisition area to the number it determines to be necessary to meet projected demand.

Although the Centers for Medicare & Medicaid Services concluded the bidding process for the first round of Metropolitan Statistical Areas in September 2007, in July 2008, Congress enacted Medicare Improvements for Patients and Providers Act of 2008, which retroactively delayed the implementation of competitive bidding.

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Medicare Improvements for Patients and Providers Act of 2008 also reduced Medicare prices nationwide by 9.5% beginning in 2009 for the product categories, including oxygen, that were initially included in competitive bidding.

In 2009, the Centers for Medicare & Medicaid Services implemented a new bidding process in nine Metropolitan Statistical Areas, covering approximately 9% of the Medicare oxygen market. Reimbursement rates from the re-bidding process were publicly released by the Centers for Medicare & Medicaid Services on June 30, 2010. The Centers for Medicare & Medicaid Services announced average savings of approximately 35% off the current standard Medicare payment rates in effect for the product categories included in competitive bidding. As of January 1, 2011, these payment rates were in effect in the nine markets only. We were offered six three-year contracts to provide oxygen equipment in six of the nine markets, and we accepted and signed those contracts.

The Centers for Medicare & Medicaid Services implemented the second phase of competitive bidding in an additional 100 competitive bidding areas covering approximately 50% of the Medicare oxygen market, with three-year contracts effective July 1, 2013. The Centers for Medicare & Medicaid Services announced average savings of approximately 45% off the current standard Medicare payment rates in effect for the product categories included in competitive bidding. As of July 1, 2013, these payment rates were in effect in the 100 competitive bidding areas. We were offered 89 contracts to provide oxygen equipment in 89 of the 100 Competitive Bidding Areas, and we accepted and signed those contracts.

Round one re-competes rates went into effect January 1, 2014; reimbursement rates from the re-bidding process were publicly released by the Centers for Medicare & Medicaid Services on October 1, 2013. The Centers for Medicare & Medicaid Services announced average savings of approximately 37% off the current standard Medicare payment rates in effect from the product categories included in competitive bidding. We were offered 3 contracts to provide respiratory equipment in 3 of the 9 competitive bidding areas, and we accepted and signed those contracts. We are required to be able to supply additional respiratory products such as sleep and aerosol therapy, which have lower margins than our existing products. This could have a negative impact on our financial conditions and results of operations.

The Patient Protection and Affordable Care Act legislation requires the Centers for Medicare & Medicaid Services to expand competitive bidding further to additional geographic markets or to use competitive bid pricing information to adjust the payment amounts otherwise in effect for areas that are not competitive acquisition areas by January 1, 2016.

Although we continue to monitor developments regarding the implementation of the competitive bidding program, we cannot predict the outcome of the competitive bidding program on our business when fully implemented, nor the Medicare payment rates that will be in effect in future years for the items subjected to competitive bidding, including our products. We expect that the stationary oxygen and non-delivery ambulatory oxygen payment rates will continue to fluctuate, and a large negative payment adjustment could adversely affect our business, financial conditions and results of operations.

We face intense national, regional and local competition and if we are unable to compete successfully, it could have an adverse effect on our revenue, revenue growth rate, if any, and market share.

The oxygen therapy market is a highly competitive industry. We compete with a number of manufacturers and distributors of portable oxygen concentrators, as well as providers of other oxygen therapy solutions such as home delivery of oxygen tanks or cylinders.

Our significant manufacturing competitors are Invacare Corporation, Respironics (a subsidiary of Koninklijke Philips N.V.), AirSep Corporation and SeQual Technologies (subsidiaries of Chart Industries, Inc.), Inova Labs, Inc. and

DeVilbiss Healthcare. Given the relatively straightforward regulatory path in the oxygen therapy device manufacturing market, we expect that the industry will become increasingly competitive in the future. Manufacturing companies compete for sales to providers primarily on the basis of product features, service and price.

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Lincare Inc., Apria Healthcare, Inc. Rotech Healthcare, Inc. and American HomePatient, Inc. are among the market leaders in providing oxygen therapy for many years, while the remaining oxygen therapy market is serviced by local providers. Because many oxygen therapy providers were either excluded from contracts in the Medicare competitive bidding process, or will have difficulty providing service at the prevailing Medicare reimbursement rates, we expect more industry consolidation. Oxygen therapy providers compete primarily on the basis of product features and service, rather than price, since reimbursement levels are established by Medicare and Medicaid, or by the individual determinations of private payors.

Some of our competitors are large, well-capitalized companies with greater resources than we have. As a consequence, they are able to spend more aggressively on product development, marketing, sales and other product initiatives than we can. Some of these competitors have:

- significantly greater name recognition;
- established relations with healthcare professionals, customers and third-party payors;
- established distribution networks;
- additional lines of products, and the ability to offer rebates or bundle products to offer higher discounts or other incentives to gain a competitive advantage;
- greater history in conducting research and development, manufacturing, marketing and obtaining regulatory approval for oxygen device products; and
- greater financial and human resources for product development, sales and marketing, patent litigation and customer financing.

As a result, our competitors may be able to respond more quickly and effectively than we can to new or changing opportunities, technologies, standard regulatory and reimbursement development and customer requirements. In light of these advantages that our competitors maintain, even if our technology and direct-to-consumer distribution strategy is more effective than the technology and distribution strategy of our competitors, current or potential customers might accept competitor products and services in lieu of purchasing our products. We anticipate that we will face increased competition in the future as existing companies and competitors develop new or improved products and distribution strategies and as new companies enter the market with new technologies and distribution strategies. We may not be able to compete effectively against these organizations. Our ability to compete successfully and to increase our market share is dependent upon our reputation for providing responsive, professional and high-quality products and services and achieving strong customer satisfaction. Increased competition in the future could adversely affect our revenue, revenue growth rate, margins and market share.

Healthcare reform measures may have a material adverse effect on our business and results of operations.

In the United States, the legislative landscape, particularly as it relates to healthcare regulation and reimbursement coverage, continues to evolve. In March 2010, the Patient Protection and Affordable Care Act was passed, which has the potential to substantially change health care financing by both governmental and private insurers, and significantly impact the U.S. medical device industry. As discussed above, the Patient Protection and Affordable Care Act, among other things, imposes a new excise tax, which began in 2013, on entities that manufacture, produce or import medical devices in an amount equal to 2.3% of the price for which such devices are sold in the United States, however oxygen products such as ours were exempt. In addition, as discussed above, the Patient Protection and Affordable Care Act also expands the round two of competitive bidding to a total of 91 competitive bidding areas, and by 2016, the process must be nationalized or prices in non-competitive bidding areas must be adjusted to match competitive bidding prices.

In addition, other legislative changes have been proposed and adopted in the United States since the Patient Protection and Affordable Care Act was enacted. On August 2, 2011, the Budget Control Act of 2011 among

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other things, created measures for spending reductions by Congress. A Joint Select Committee on Deficit Reduction, tasked with recommending a targeted deficit reduction of at least $1.2 trillion for the years 2013 through 2021, was unable to reach required goals, thereby triggering the legislation s automatic reduction to several government programs. This includes aggregate reductions of Medicare payments to providers up to 2% per fiscal year, which went into effect on April 1, 2013. On January 2, 2013, President Obama signed into law the American Taxpayer Relief Act of 2012 which, among other things, further reduced Medicare payments to certain providers, including physicians, hospitals, imaging centers and cancer treatment centers, and increased the statute of limitations period for the government to recover overpayments to providers from three to five years. We expect that additional state and federal healthcare reform measures will be adopted in the future, any of which could limit the amounts that federal and state governments will pay for healthcare products and services, which could result in reduced demand for our products or additional pricing pressures.

If we are unable to continue to enhance our existing products and develop and market new products that respond to customer needs and preferences and achieve market acceptance, we may experience a decrease in demand for our products and our business could suffer.

We may not be able to compete as effectively with our competitors, and ultimately satisfy the needs and preferences of our customers, unless we can continue to enhance existing products and develop new innovative products. Product development requires significant financial, technological, and other resources. While we expended $2.3 million and $2.4 million for research and development efforts in 2012 and 2013, respectively, we cannot assure you that this level of investment in research and development will be sufficient to maintain a competitive advantage in product innovation, which could cause our business to suffer. Product improvements and new product introductions also require significant planning, design, development, and testing at the technological, product, and manufacturing process levels and we may not be able to timely develop product improvements or new products. Our competitors new products may beat our products to market, be more effective with more features, obtain better market acceptance, or render our products obsolete. Any new products that we develop may not receive market acceptance or otherwise generate any meaningful sales or profits for us relative to our expectations based on, among other things, existing and anticipated investments in manufacturing capacity and commitments to fund advertising, marketing, promotional programs, and research and development.

We depend upon reimbursement from Medicare, private payors and Medicaid for a significant portion of our revenue, and if we fail to manage the complex and lengthy reimbursement process, our business and operating results could suffer.

A significant portion of our revenue is derived from reimbursement by third-party payors. We accept assignment of insurance benefits from customers and, in a majority of cases, invoice and collect payments directly from Medicare, private payors and Medicaid, as well as from customers under co-insurance provisions. In 2013, approximately 41% of our revenue was derived from Medicare, private payors, Medicaid, and individual customers from rental revenue which receives reimbursement payment.

Our financial condition and results of operations may be affected by the health care industry s reimbursement process, which is complex and can involve lengthy delays between the time that a product is delivered to the consumer and the time that the reimbursement amounts are settled. Depending on the payor, we may be required to obtain certain payor-specific documentation from physicians and other health care providers before submitting claims for reimbursement. Certain payors have filing deadlines and they will not pay claims submitted after such time. We are also subject to extensive pre-payment and post-payment audits by governmental and private payors that could result in material delays, refunds of monies received or denials of claims submitted for payment under such third-party payor programs and contracts. We cannot ensure that we will be able to continue to effectively manage the reimbursement

process and collect payments for our products promptly. If we fail to manage the complex and lengthy reimbursement process, it would adversely affect our business, financial conditions, and results of operations.

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Failure to obtain private payor contracts and future reductions in reimbursement rates from private payors could have a material adverse effect on our financial condition and operating results.

A portion of our revenue is derived from private payors. Based on our patient population, we estimate at least 30% of potential customers have non-Medicare insurance coverage, and we believe these patients represent a younger and more active patient population that will be drawn to the quality-of-life benefits of our solution. Failing to maintain and obtain private payor contracts from private insurance companies and employers and secure in-network provider status could have a material adverse effect on our financial condition and operating results. In addition, private payors are under pressure to increase profitability and reduce costs. In response, certain private payors are limiting coverage or reducing reimbursement rates for the products we provide. We believe that private payor reimbursement levels will generally be reset in accordance with the Medicare payment amounts determined by competitive bidding. We cannot predict the extent to which reimbursement for our products will be affected by competitive bidding or by initiatives to reduce costs for private payors. Failure to obtain or maintain private payor contracts or the unavailability of third-party coverage or inadequacy of reimbursement for our products would adversely affect our business, financial conditions, and results of operations.

We obtain some of the components, subassemblies and completed products included in our Inogen One systems from a single source or a limited group of manufacturers or suppliers, and the partial or complete loss of one of these manufacturers or suppliers could cause significant production delays, an inability to meet customer demand and a substantial loss in revenue.

We utilize single source suppliers for some of the components and subassemblies we use in our Inogen One systems. We have qualified alternate sources of supply sufficient to support future needs and we have taken other mitigating steps to reduce the impact of a change in supplier; however, there may be delays in switching to these alternative suppliers if our primary source is terminated without notice. Our dependence on single source suppliers of components may expose us to several risks, including, among other things:

Our suppliers may encounter financial hardships as a result of unfavorable economic and market conditions unrelated to our demand for components, which could inhibit their ability to fulfill our orders and meet our requirements;

Suppliers may fail to comply with regulatory requirements, be subject to lengthy compliance, validation or qualification periods, or make errors in manufacturing components that could negatively affect the efficacy or safety of our products or cause delays in supplying of our products to our customers;

Newly identified suppliers may not qualify under the stringent regulatory standards to which our business is subject;

We or our suppliers may not be able to respond to unanticipated changes in customer orders, and if orders do not match forecasts, we or our suppliers may have excess or inadequate inventory of materials and components;

We may be subject to price fluctuations due to a lack of long-term supply arrangements for key components;

We may experience delays in delivery by our suppliers due to changes in demand from us or their other customers;

We or our suppliers may lose access to critical services and components, resulting in an interruption in the manufacture, assembly and shipment of our systems;

Our suppliers may be subject to allegations by other parties of misappropriation of proprietary information in connection with their supply of products to us, which could inhibit their ability to fulfill our orders and meet our requirements;

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Fluctuations in demand for products that our suppliers manufacture for others may affect their ability or willingness to deliver components to us in a timely manner;

Our suppliers may wish to discontinue supplying components or services to us; and

We may not be able to find new or alternative components or reconfigure our system and manufacturing processes in a timely manner if the necessary components become unavailable.

In addition, we may be deemed to manufacture or contract to manufacture products that contain certain minerals that have been designated as conflict minerals under the Dodd-Frank Wall Street Reform and Consumer Protection Act. As a result, in future periods, we may be required to diligence the origin of such minerals and disclose and report whether or not such minerals originated in the Democratic Republic of the Congo or adjoining countries. The implementation of these new requirements could adversely affect the sourcing, availability, and pricing of minerals used in the manufacture of our products. In addition, we may incur additional costs to comply with the disclosure requirements, including costs related to determining the source of any of the relevant minerals and metals used in our products.

If any of these risks materialize, costs could significantly increase and our ability to meet demand for our products could be impacted. If we are unable to satisfy commercial demand for our Inogen One systems in a timely manner, our ability to generate revenue would be impaired, market acceptance of our products could be adversely affected, and customers may instead purchase or use alternative products. In addition, we could be forced to secure new or alternative components and subassemblies through a replacement supplier. Finding alternative sources for these components and subassemblies could be difficult in certain cases and may entail a significant amount of time and disruption. In some cases, we would need to change the components or subassemblies if we sourced them from an alternative supplier. This, in turn, could require a redesign of our Inogen One systems and, potentially, require additional FDA clearance or approval before we could use any redesigned product with new components or subassemblies, thereby causing further costs and delays that could adversely affect our business, financial condition and operating results.

We do not have long-term supply contracts with many of our third-party suppliers.

We purchase components and subassemblies from third-party suppliers, including some of our single source suppliers, through purchase orders and do not have long-term supply contracts with many of these third-party suppliers. Many of our third-party suppliers, therefore, are not obligated to perform services or supply products to us for any specific period, in any specific quantity or at any specific price, except as may be provided in a particular purchase order. We do not maintain large volumes of inventory from most of these suppliers. If we inaccurately forecast demand for components or subassemblies, our ability to manufacture and commercialize our Inogen One systems could be delayed and our competitive position and reputation could be harmed. In addition, if we fail to effectively manage our relationships with these suppliers, we may be required to change suppliers which would be time consuming and disruptive and could adversely affect our business, financial condition and operating results.

If we fail to comply with U.S. export control and economic sanctions or fail to expand and maintain an effective sales force or successfully develop our international distribution network, our business, financial condition and operating results may be adversely affected.

We currently derive the majority of our revenue from rentals or sales generated from our own direct sales force. Failure to maintain or expand our direct sales force could adversely impact our financial and operating performance.

Additionally, we use international distributors to augment our sales efforts, certain of which are exclusive distributors in certain foreign countries. We cannot assure you that we will be able to successfully develop our relationships with third-party distributors internationally. In addition, we are subject to United States export control and economic sanctions laws relating to the sale of our products, the violation of which could result in substantial penalties being imposed against us. In particular, we have secured annual export licenses from the U.S. Treasury Department s Office of Foreign Assets Control to sell our products to a distributor and

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hospital and clinic end-users in Iran. The use of this license requires us to observe strict conditions with respect to products sold, end-user limitations and payment requirements. Although we believe we have maintained compliance with license requirements, there can be no assurance that the license will not be revoked, be renewed in the future or that we will remain in compliance. More broadly, if we fail to comply with export control laws or successfully develop our relationship with international distributors, our sales could fail to grow or could decline, and our ability to grow our business could be adversely affected. Distributors that are in the business of selling other medical products may not devote a sufficient level of resources and support required to generate awareness of our products and grow or maintain product sales. If our distributors are unwilling or unable to market and sell our products, or if they do not perform to our expectations, we could experience delayed or reduced market acceptance and sales of our products.

We may be subject to substantial warranty or product liability claims or other litigation in the ordinary course of business that may adversely affect our business, financial condition and operating results.

As manufacturers of medical devices, we may be subject to substantial warranty or product liability claims or other litigation in the ordinary course of business that may require us to make significant expenditures to defend these claims or pay damage awards. For example, our Inogen One systems contain lithium ion batteries, which, under certain circumstances, can be a fire hazard. We, as well as our key suppliers, maintain product liability insurance, but this insurance is limited in amount and subject to significant deductibles. There is no guarantee that insurance will be available or adequate to protect against all claims. Our insurance policies are subject to annual renewal and we may not be able to obtain liability insurance in the future on acceptable terms or at all. In addition, our insurance premiums could be subject to increases in the future, which may be material. If the coverage limits are inadequate to cover our liabilities or our insurance costs continue to increase as a result of warranty or product liability claims or other litigation, then our business, financial condition and operating results may be adversely affected.

Increases in our operating costs could have a material adverse effect on our business, financial condition and operating results.

Reimbursement rates are established by fee schedules mandated by Medicare, private payors and Medicaid are likely to remain constant or decrease due, in part, to federal and state government budgetary constraints. As a result, with respect to Medicare and Medicaid related revenue, we are not able to offset the effects of general inflation on our operating costs through increases in prices for our products. In particular, labor and related costs account for a significant portion of our operating costs and we compete with other health care providers to attract and retain qualified or skilled personnel and with various industries for administrative and service employees. This competitive environment could result in increased labor costs. As such, we must control our operating costs, particularly labor and related costs, and failing to do so could adversely affect our financial conditions and results of operations.

We depend on the services of our senior executives and other key technical personnel, the loss of whom could negatively affect our business.

Our success depends upon the skills, experience and efforts of our senior executives and other key technical personnel, including certain members of our engineering staff, and our sales and marketing executives. Much of our corporate expertise is concentrated in relatively few employees, the loss of which for any reason could negatively affect our business. Competition for our highly skilled employees is intense and we cannot prevent the resignation of any employee. We do not maintain key man life insurance on any of our senior executives. None of our senior executive team is bound by written employment contracts to remain with us for a specified period. In addition, we have not entered into non-compete agreements with members of our senior management team. The loss of any member of our senior management team could harm our ability to implement our business strategy and respond to the market conditions in which we operate.

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We have incurred losses since inception until fiscal year 2012, and we have only recently achieved profitability.

We have a limited operating history and have incurred significant net losses in each fiscal year until fiscal year 2012, when we achieved positive net income. As of December 31, 2013, we had an accumulated deficit of $62.6 million. These net losses have resulted principally from costs incurred in our research and development programs and from our selling, general and administrative expenses. We expect to incur increases in expenses for research and development and significant expansion of our sales and marketing capabilities. Additionally, since completing our initial public offering, we expect that our selling, general and administrative expenses will increase due to the additional operational and reporting costs associated with being a public company. Because of the numerous risks and uncertainties associated with our commercialization efforts and future product development, we are unable to predict if we will maintain or increase our net income.

Our financial results may vary significantly from quarter-to-quarter due to a number of factors, which may lead to volatility in our stock price.

Our quarterly revenue and results of operations have varied in the past and may continue to vary significantly from quarter-to-quarter. This variability may lead to volatility in our stock price as research analysts and investors respond to these quarterly fluctuations. These fluctuations are due to numerous factors, including: fluctuations in consumer demand for our products; seasonal cycles in consumer spending; our ability to design, manufacture and deliver products to our consumers in a timely and cost-effective manner; quality control problems in our manufacturing operations; our ability to timely obtain adequate quantities of the components used in our products; new product introductions and enhancements by us and our competitors; unanticipated increases in costs or expenses; and fluctuations in foreign currency exchange rates. For example, we typically experience higher sales in the second quarter, as a result of consumers traveling and vacationing during the summer months. The foregoing factors are difficult to forecast, and these, as well as other factors, could materially and adversely affect our quarterly and annual results of operations. In addition, a significant amount of our operating expenses are relatively fixed due to our manufacturing, research and development, and sales and general administrative efforts. Any failure to adjust spending quickly enough to compensate for a revenue shortfall could magnify the adverse impact of such revenue shortfall on our results of operations. Our results of operations may not meet the expectations of research analysts or investors, in which case the price of our common stock could decrease significantly.

The terms of our revolving credit and term loan agreement may restrict our current and future operations, and could affect our ability to respond to changes in our business and to manage our operations.

We are parties to an amended and restated revolving credit and term loan agreement with Comerica Bank as administrative agent, which we refer to as our revolving credit and term loan agreement. The agreement provides for a previously existing term loan in the amount of $3.0 million, another previously existing term loan in the amount of $8.0 million and a new term loan facility in the amount of $12.0 million. As of December 31, 2013, we had term loan borrowings outstanding under the agreement of $9.9 million, which included $0.4 million and $3.8 million under the pre-existing term loans, and $5.7 million under the new term loan. The agreement also provides for a $1.0 million revolving line of credit, none of which was outstanding as of December 31, 2013. The revolver expired on October 13, 2013 and we have no plans to renew or replace it. The agreement is secured by all or substantially all of our assets.

Pursuant to the agreement, we are subject to certain financial covenants relating to liquidity, debt service, and leverage ratios. The liquidity ratio is the ratio of (i) liquidity (cash plus eligible accounts receivable) to (ii) the current portion of all indebtedness owed to the lenders. The debt service coverage ratio is the ratio on a basis of (a) Adjusted EBITDA, less (i) cash capital expenditures (including rental equipment) and (ii) taxes paid or payable, to (b) the sum of cash principal payments plus interest expense paid or payable, all such items in clauses (a) and (b) measured on an

annualized trailing six (6) months basis; provided that cash capital

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expenditures shall not be subtracted from clause (a) hereof so long as we maintain at least $1.5 million in unrestricted cash during the entire relevant fiscal period. The senior leverage ratio is the ratio of (a) funded debt basis to (b) Adjusted EBITDA measured on an annualized trailing six (6) months basis.

The agreement contains events of default customary for transactions of this type, including nonpayment, misrepresentation, breach of covenants, material adverse effect and bankruptcy. As of December 31, 2013, we had no outstanding balance under the revolving line of credit and an outstanding balance of $9.9 million under the term loan. In the event we fail to satisfy our covenants, or otherwise go into default, Comerica Bank has a number of remedies, including sale of our assets and acceleration of all outstanding indebtedness. Certain of these remedies would likely have a material adverse effect on our business. As of December 31, 2013, in order to be in compliance with the liquidity requirements, debt service ratios, and leverage ratios of existing debt obligations, we were required to maintain $2.5 million in unaudited Adjusted EBITDA in the previous six months, and we had $6.5 million in actual unaudited Adjusted EBITDA, and $18.7 million of cash and qualified accounts receivable, and we had $13.5 million of actual cash.

An adverse outcome of a sales and use tax audit could have a material adverse effect on our results of operations and financial condition.

The California State Board of Equalization conducted a sales and use tax audit of our operations in California in 2008. As a result of the audit, the California State Board of Equalization confirmed that our sales are not subject to California sales and use tax. We believe that our sales in other states should not be subject to sales and use tax. There can be no assurance, however, that other states may agree with our position and we may be subject to an audit that may not be resolved in our favor. Such an audit could be expensive and time-consuming and result in substantial management distraction. If the matter were to be resolved in a manner adverse to us, it could have a material adverse effect on our results of operations and financial position.

Our ability to use net operating losses to offset future taxable income may be subject to certain limitations.

As of December 31, 2013, we had federal and state net operating loss carryforwards, or NOLs, of approximately $57.0 and 55.0 million, which expire in various years beginning in 2022 and 2013, if not utilized. In general, under Section 382 of the Internal Revenue Code of 1986, as amended, or the Code, a corporation that undergoes an ownership change is subject to limitations on its ability to utilize its pre-change NOLs to offset future taxable income. In general, an ownership change occurs if there is a cumulative change in our ownership by 5% shareholders that exceeds 50 percentage points over a rolling three-year period. Our existing NOLs may be subject to limitations arising from previous ownership changes, and if we undergo one or more ownership changes our ability to utilize NOLs could be further limited by Section 382 of the Code. Even after factoring in these limitations, the company was able to determine based on future projections of income that it is more likely than not that all of its federal NOL s will be utilized before they expire and therefore determined that releasing the valuation allowance relating to these NOL s was appropriate during this period. However, the company determined that some of its California NOL s will expire unused and therefore has maintained a valuation allowance of $4.1M relating to these NOL s.

Risks related to the regulatory environment

We are subject to extensive federal and state regulation, and if we fail to comply with applicable regulations, we could suffer severe criminal or civil sanctions or be required to make significant changes to our operations that could adversely affect our business, financial condition and operating results.

The federal government and all states in which we currently operate regulate various aspects of our business. In particular, our sales and customer service centers are subject to federal laws that regulate interstate motor-carrier transportation. Our operations also are subject to state laws governing, among other things, distribution of medical equipment and certain types of home health activities, and we are required to obtain and maintain licenses in each state to act as a durable medical equipment supplier. Certain of our employees are subject to state laws and regulations governing the professional practices of respiratory therapy.

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As a health care provider participating in governmental healthcare programs, we are subject to laws directed at preventing fraud and abuse, which subject our marketing, billing, documentation and other practices to government scrutiny. To ensure compliance with Medicare, Medicaid and other regulations, government agencies or their contractors often conduct routine audits and request customer records and other documents to support our claims submitted for payment of services rendered. Government agencies or their contractors also periodically open investigations and obtain information from health care providers. Violations of federal and state regulations can result in severe criminal, civil and administrative penalties and sanctions, including debarment, suspension or exclusion from Medicare, Medicaid and other government reimbursement programs, any of which would have a material adverse effect on our business.

Changes in healthcare laws and regulations and new interpretations of existing laws and regulations may affect permissible activities, the relative costs associated with doing business, and reimbursement amounts paid by federal, state and other third-party payors. There have been and will continue to be regulatory initiatives affecting our business and we cannot predict the extent to which future legislation and regulatory changes could have a material adverse effect on our business.

We are subject to burdensome and complex billing and record-keeping requirements in order to substantiate our claims for payment under federal, state and commercial health care reimbursement programs, and our failure to comply with existing requirements, or changes in those requirements or interpretations thereof, could adversely affect our business, financial condition and operating results.

We are subject to burdensome and complex billing and record-keeping requirements in order to substantiate our claims for payment under federal, state and commercial health care reimbursement programs. Our records also are subject to routine and other reviews by third-party payors, which can result in delays in payments or refunds of paid claims. For example, we have also experienced a significant increase in pre-payment reviews of our claims by the Durable Medical Equipment Medicare Administrative Contractors, which has caused substantial delays in the collection of our Medicare accounts receivable as well as related amounts due under supplemental insurance plans.

Current law provides for a significant expansion of the government s auditing and oversight of suppliers who care for patients covered by various government health care programs. Examples of this expansion include audit programs being implemented by the Durable Medical Equipment Medicare Administrative Contractors, the Zone Program Integrity Contractors, the Recovery Audit Contractors, and the Comprehensive Error Rate Testing contractors, operating under the direction of the Centers for Medicare & Medicaid Services.

We have been informed by these auditors that health care providers and suppliers of certain durable medical equipment product categories are expected to experience further increased scrutiny from these audit programs. When a government auditor ascribes a high billing error rate to one or more of our locations, it generally results in protracted pre-payment claims review, payment delays, refunds and other payments to the government and/or our need to request more documentation from providers than has historically been required. It may also result in additional audit activity in other company locations in that state or Durable Medical Equipment Medicare Administrative Contractors jurisdiction. We cannot currently predict the adverse impact that these audits, methodologies and interpretations might have on our business, financial condition or operating results, but such impact could be material.

We are subject to significant regulation by numerous government agencies, including the U.S. Food and Drug Administration, or FDA. We cannot market or commercially distribute our products without obtaining and maintaining necessary regulatory clearances or approvals.

Our Inogen One systems are medical devices subject to extensive regulation in the United States and in the foreign markets where we distribute our products. The FDA and other U.S. and foreign governmental agencies regulate, among other things, with respect to medical devices:

design, development and manufacturing;

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testing, labeling, content and language of instructions for use and storage;

clinical trials;

product safety;

marketing, sales and distribution;

pre-market clearance and approval;

record keeping procedures;

advertising and promotion;

recalls and field safety corrective actions;

post-market surveillance, including reporting of deaths or serious injuries and malfunctions that, if they were to recur, could lead to death or serious injury;

post-market approval studies; and

product import and export.

Before we can market or sell a medical device in the United States, we must obtain either clearance from the FDA under Section 510(k) of the Federal Food, Drug, and Cosmetic Act, or the FDCA, or approval of a pre-market approval, application from the FDA, unless an exemption from pre-market review applies. In the 510(k) clearance process, the FDA must determine that a proposed device is substantially equivalent to a device legally on the market, known as a predicate device, with respect to intended use, technology and safety and effectiveness, in order to clear the proposed device for marketing. Clinical data is sometimes required to support substantial equivalence. The pre-market approval pathway requires an applicant to demonstrate the safety and effectiveness of the device based, in part, on extensive data, including, but not limited to, technical, preclinical, clinical trial, manufacturing and labeling data. The pre-market approval process is typically required for devices that are deemed to pose the greatest risk, such as life-sustaining, life-supporting or implantable devices. Products that are approved through a pre-market approval application generally need FDA approval before they can be modified. Similarly, some modifications made to products cleared through a 510(k) may require a new 510(k). Both the 510(k) and pre-market approval processes can be expensive and lengthy and require the payment of significant fees, unless an exemption applies. The FDA s 510(k) clearance process usually takes from three to 12 months, but may take longer. The process of obtaining a pre-market approval is much more costly and uncertain than the 510(k) clearance process and generally takes from one to three years, or longer, from the time the application is submitted to the FDA until an approval is obtained. The process of

obtaining regulatory clearances or approvals to market a medical device can be costly and time consuming, and we may not be able to obtain these clearances or approvals on a timely basis, if at all.

In the United States, our currently commercialized products are marketed pursuant to pre-market clearance under Section 510(k) of the FDCA. If the FDA requires us to go through a lengthier, more rigorous examination for future products or modifications to existing products than we had expected, our product introductions or modifications could be delayed or canceled, which could cause our sales to decline. In addition, the FDA may determine that future products will require the more costly, lengthy and uncertain pre-market approval process. Although we do not currently market any devices under a pre-market approval, the FDA may demand that we obtain a pre-market approval prior to marketing certain of our future products. In addition, if the FDA disagrees with our determination that a product we currently market is subject to an exemption from pre-market review, the FDA may require us to submit a 510(k) or pre-market approval application in order to continue marketing the product. Further, even with respect to those future products where a pre-market approval is not required, we cannot assure you that we will be able to obtain the 510(k) clearances with respect to those products.

The FDA can delay, limit or deny clearance or approval of a device for many reasons, including:

- we may not be able to demonstrate to the FDA s satisfaction that our products are safe and effective for their intended users;

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the data from our pre-clinical studies and clinical trials may be insufficient to support clearance or approval, where required; and

the manufacturing process or facilities we use may not meet applicable requirements.

In addition, the FDA may change its clearance and approval policies, adopt additional regulations or revise existing regulations, or take other actions which may prevent or delay approval or clearance of our products under development or impact our ability to modify our currently approved or cleared products on a timely basis. For example, in response to industry and healthcare provider concerns regarding the predictability, consistency and rigor of the 510(k) regulatory pathway, the FDA initiated an evaluation of the program, and in January 2011, announced several proposed actions intended to reform the review process governing the clearance of medical devices. The FDA intends these reform actions to improve the efficiency and transparency of the clearance process, as well as bolster patient safety. Some of these proposals, if enacted, could impose additional regulatory requirements upon us which could delay our ability to obtain new 510(k) clearances, increase the costs of compliance or restrict our ability to maintain our current clearances. In addition, as part of the Food and Drug Administration Safety and Innovation Act, Congress reauthorized the Medical Device User Fee Amendments with various FDA performance goal commitments and enacted several Medical Device Regulatory Improvements and miscellaneous reforms which are further intended to clarify and improve medical device regulation both pre- and post-market.

Medical devices may only be promoted and sold for the indications for which they are approved or cleared. In addition, even if the FDA has approved or cleared a product, it can take action affecting such product approvals or clearances if serious safety or other problems develop in the marketplace. Delays in obtaining clearances or approvals could adversely affect our ability to introduce new products or modifications to our existing products in a timely manner, which would delay or prevent commercial sales of our products. Additionally, the FDA and other regulatory authorities have broad enforcement powers. Regulatory enforcement or inquiries, or other increased scrutiny on us, could affect the perceived safety and efficacy of our products and dissuade our customers from using our products.

If we modify our FDA cleared devices, we may need to seek additional clearances or approvals, which, if not granted, would prevent us from selling our modified products.

Our Inogen One systems have received pre-market clearance under Section 510(k) of the FDCA. The modifications made to our Inogen One G2 and Inogen One G3 systems represent non-significant modifications to the original Inogen One system, have the same indications for use, and are covered under our initial Inogen One 510(k) clearance. Any modifications to a 510(k)-cleared device that could significantly affect its safety or effectiveness, or would constitute a major change in its intended use, manufacture, design, components, or technology requires the submission and clearance of a new 510(k) pre-market notification or, possibly, pre-market approval. The FDA requires every manufacturer to make this determination in the first instance, but the FDA may review any manufacturer s decision. The FDA may not agree with our decisions regarding whether new clearances or approvals are necessary. We have modified some of our 510(k) cleared products, and have determined based on our review of the applicable FDA guidance that in certain instances new 510(k) clearances or pre-market approval are not required. If the FDA disagrees with our determination and requires us to submit new 510(k) notifications or pre-market approval for modifications to our previously cleared products for which we have concluded that new clearances or approvals are unnecessary, we may be required to cease marketing or to recall the modified product until we obtain clearance or approval, and we may be subject to significant regulatory fines or penalties.

Furthermore, the FDA s ongoing review of the 510(k) program may make it more difficult for us to make modifications to our previously cleared products, either by imposing more strict requirements on when a manufacturer must submit a new 510(k) for a modification to a previously cleared product, or by applying more onerous review

criteria to such submissions. Specifically, pursuant to the Food and Drug Administration Safety and Innovation Act, which was signed into law in July 2012, the FDA is obligated to prepare a report for

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Congress on the FDA s approach for determining when a new 510(k) will be required for modifications or changes to a previously cleared device. After submitting this report, the FDA is expected to issue revised guidance to assist device manufacturers in making this determination. Until then, manufacturers may continue to adhere to the FDA s 1997 guidance on this topic when making a determination as to whether or not a new 510(k) is required for a change or modification to a device, but the practical impact of the FDA s continuing scrutiny of these issues remains unclear.

If we fail to comply with FDA or state regulatory requirements, we can be subject to enforcement action.

The regulations to which we are subject are complex and have become more stringent over time. Regulatory changes could result in restrictions on our ability to continue or expand our operations, higher than anticipated costs or lower than anticipated sales. Even after we have obtained the proper regulatory clearance or approval to market a product, we have ongoing responsibilities under FDA regulations. The FDA and state authorities have broad enforcement powers. Our failure to comply with applicable regulatory requirements could result in enforcement action by the FDA or state agencies, which may include any of the following sanctions:

warning letters, fines, injunctions, consent decrees and civil penalties;

recalls, termination of distribution, or seizure of our products;

operating restrictions or partial suspension or total shutdown of production;

delays in the introduction of products into the market;

refusal to grant our requests for future 510(k) clearances or approvals of new products, new intended uses, or modifications to exiting products;

withdrawals or suspensions of current 510(k) clearances or approvals, resulting in prohibitions on sales of our products; and

criminal prosecution.

Any of these sanctions could result in higher than anticipated costs or lower than anticipated sales and have a material adverse effect on our reputation, business, results of operations and financial condition.

A recall of our products, either voluntarily or at the direction of the FDA or another governmental authority, or the discovery of serious safety issues with our products that leads to corrective actions, could have a significant adverse impact on us.

Medical devices, such as our Inogen One systems, can experience performance problems in the field that require review and possible corrective action by us or the product manufacturer. We cannot provide assurance that component failures, manufacturing errors, design defects and/or labeling inadequacies, which could result in an unsafe condition

or injury to the operator or the patient will not occur. The FDA and similar foreign governmental authorities have the authority to require the recall of commercialized products in the event of material deficiencies or defects in design or manufacture of a product or in the event that a product poses an unacceptable risk to health. Manufacturers may also, under their own initiative, recall a product if any material deficiency in a device is found or withdraw a product to improve device performance or for other reasons. A government-mandated or voluntary recall by us or one of our distributors could occur as a result of an unacceptable risk to health, component failures, manufacturing errors, design or labeling defects or other deficiencies and issues. Similar regulatory agencies in other countries have similar authority to recall devices because of material deficiencies or defects in design or manufacture that could endanger health. Any recall would divert management attention and financial resources, could cause the price of our stock to decline and expose us to product liability or other claims and harm our reputation with customers. A recall involving our Inogen One systems could be particularly harmful to our business, financial and operating results.

In addition, under the FDA s medical device reporting regulations, we are required to report to the FDA any incident in which our product may have caused or contributed to a death or serious injury or in which our product

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malfunctioned and, if the malfunction were to recur, would likely cause or contribute to death or serious injury. Repeated product malfunctions may result in a voluntary or involuntary product recall. Depending on the corrective action we take to redress a product s deficiencies or defects, the FDA may require, or we may decide, that we will need to obtain new approvals or clearances for the device before we may market or distribute the corrected device. Seeking such approvals or clearances may delay our ability to replace the recalled devices in a timely manner. Moreover, if we do not adequately address problems associated with our devices, we may face additional regulatory enforcement action, including FDA warning letters, product seizure, injunctions, administrative penalties, or civil or criminal fines. We may also be required to bear other costs or take other actions that may have a negative impact on our sales as well as face significant adverse publicity or regulatory consequences, which could harm our business, including our ability to market our products in the future.

Any adverse event involving our products, whether in the United States or abroad, could result in future voluntary corrective actions, such as recalls or customer notifications, or agency action, such as inspection, mandatory recall or other enforcement action. Any corrective action, whether voluntary or involuntary, as well as defending ourselves in a lawsuit, will require the dedication of our time and capital, distract management from operating our business and may harm our reputation and financial results.

If we or our component manufacturers fail to comply with the FDA s Quality System Regulation, our manufacturing operations could be interrupted, and our product sales and operating results could suffer.

We and our component manufacturers are required to comply with the FDA s Quality System Regulation, or QSR, which covers the procedures and documentation of the design, testing, production, control, quality assurance, labeling, packaging, sterilization, storage and shipping of our devices. The FDA audits compliance with the QSR through periodic announced and unannounced inspections of manufacturing and other facilities. We and our component manufacturers have been, and anticipate in the future being, subject to such inspections. Although we believe our manufacturing facilities and those of our component manufacturers are in compliance with the QSR, we cannot provide assurance that any future inspection will not result in adverse findings. If our manufacturing facilities or those of any of our component manufacturers or suppliers are found to be in violation of applicable laws and regulations, or we or our manufacturers or suppliers fail to take satisfactory corrective action in response to an adverse inspection, the FDA could take enforcement action, including any of the following sanctions:

- untitled letters, warning letters, fines, injunctions, consent decrees and civil penalties;
- customer notifications or repair, replacement, refunds, recall, detention or seizure of our products;
- operating restrictions or partial suspension or total shutdown of production;
- refusing or delaying our requests for 510(k) clearance or pre-market approval of new products or modified products;
- withdrawing 510(k) clearances or pre-market approvals that have already been granted;

refusal to grant export approval for our products; or

criminal prosecution.

Any of these sanctions could adversely affect our business, financial conditions and operating results.

Outside the United States, our products and operations are also often required to comply with standards set by industrial standards bodies, such as the International Organization for Standardization, or ISO. Foreign regulatory bodies may evaluate our products or the testing that our products undergo against these standards. The specific standards, types of evaluation and scope of review differ among foreign regulatory bodies. If we fail to adequately comply with any of these standards, a foreign regulatory body may take adverse actions similar to those within the power of the FDA. Any such action may harm our reputation and could have an adverse effect on our business, results of operations and financial condition.

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If we fail to obtain and maintain regulatory approval in foreign jurisdictions, our market opportunities will be limited.

Approximately 22% of our revenue was from sales outside of the United States in 2013. We sell our products in 43 countries outside of the United States through distributors or directly to large house accounts. In order to market our products in the European Union or other foreign jurisdictions, we must obtain and maintain separate regulatory approvals and comply with numerous and varying regulatory requirements. The approval procedure varies from country to country and can involve additional testing. The time required to obtain approval abroad may be longer than the time required to obtain FDA clearance. The foreign regulatory approval process includes many of the risks associated with obtaining FDA clearance and we may not obtain foreign regulatory approvals on a timely basis, if at all. FDA clearance does not ensure approval by regulatory authorities in other countries, and approval by one foreign regulatory authority does not ensure approval by regulatory authorities in other foreign countries. However, the failure to obtain clearance or approval in one jurisdiction may have a negative impact on our ability to obtain clearance or approval elsewhere. If we do not obtain or maintain necessary approvals to commercialize our products in markets outside the United States, it would negatively affect our overall market penetration.

We may be subject to fines, penalties or injunctions if we are determined to be promoting the use of our products for unapproved or off-label uses, resulting in damage to our reputation and business.

Our promotional materials and training methods must comply with FDA and other applicable laws and regulations, including the prohibition of the promotion of a medical device for a use that has not been cleared or approved by the FDA. Use of a device outside its cleared or approved indications is known as off-label use. Physicians may use our products off-label, as the FDA does not restrict or regulate a physician s choice of treatment within the practice of medicine. If the FDA determines that our promotional materials or training constitutes promotion of an off-label use, it could request that we modify our training or promotional materials or subject us to regulatory or enforcement actions, which could have an adverse impact on our reputation and financial results.

Failure to comply with the Federal Health Insurance Portability and Accountability Act of 1996, or HIPAA, the Health Information Technology for Economic and Clinical Health Act, or HITECH Act, and implementing regulations (including the final omnibus rule published on January 25, 2013) affecting the transmission, security and privacy of health information could result in significant penalties.

Numerous federal and state laws and regulations, including HIPAA and the HITECH Act, govern the collection, dissemination, security, use and confidentiality of patient-identifiable health information. HIPAA and the HITECH Act require us to comply with standards for the use and disclosure of health information within our company and with third parties. The Privacy Standards and Security Standards under HIPAA establish a set of basic national privacy and security standards for the protection of individually identifiable health information by health plans, healthcare clearinghouses and certain healthcare providers, referred to as covered entities, and the business associates with whom such covered entities contract for services. Notably, whereas HIPAA previously directly regulated only these covered entities, the HITECH Act, which was signed into law as part of the stimulus package in February 2009, makes certain of HIPAA s privacy and security standards also directly applicable to covered entities business associates. As a result, both covered entities and business associates are now subject to significant civil and criminal penalties for failure to comply with Privacy Standards and Security Standards.

HIPAA and the HITECH Act also include standards for common health care electronic transactions and code sets, such as claims information, plan eligibility, payment information and the use of electronic signatures, and privacy and electronic security of individually identifiable health information. Covered entities, such as health care providers, are required to conform to such transaction set standards pursuant to HIPAA.

HIPAA requires health care providers like us to develop and maintain policies and procedures with respect to protected health information that is used or disclosed, including the adoption of administrative, physical and

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technical safeguards to protect such information. The HITECH Act expands the notification requirement for breaches of patient-identifiable health information, restricts certain disclosures and sales of patient-identifiable health information and provides a tiered system for civil monetary penalties for HIPAA violations. The HITECH Act also increased the civil and criminal penalties that may be imposed against covered entities, business associates and possibly other persons and gave state attorneys general new authority to file civil actions for damages or injunctions in federal courts to enforce the federal HIPAA laws and seek attorney fees and costs associated with pursuing federal civil actions. Additionally, certain states have adopted comparable privacy and security laws and regulations, some of which may be more stringent than HIPAA.

If we do not comply with existing or new laws and regulations related to patient health information, we could be subject to criminal or civil sanctions. New health information standards, whether implemented pursuant to HIPAA, the HITECH Act, congressional action or otherwise, could have a significant effect on the manner in which we handle health care related data and communicate with payors, and the cost of complying with these standards could be significant.

The 2013 final HITECH omnibus rule modifies the breach reporting standard in a manner that will likely make more data security incidents qualify as reportable breaches. Any liability from a failure to comply with the requirements of HIPAA or the HITECH Act could adversely affect our financial condition. The costs of complying with privacy and security related legal and regulatory requirements are burdensome and could have a material adverse effect on our results of operations. These new provisions, as modified, will be subject to interpretation by various courts and other governmental authorities, thus creating potentially complex compliance issues for us, as well as our clients and strategic partners. In addition, we are unable to predict what changes to the HIPAA Privacy Standards and Security Standards might be made in the future or how those changes could affect our business. Any new legislation or regulation in the area of privacy and security of personal information, including personal health information, could also adversely affect our business operations.

Regulations requiring the use of standard transactions for healthcare services issued under HIPAA may negatively impact our profitability and cash flows.

Pursuant to HIPAA, final regulations have been implemented to improve the efficiency and effectiveness of the healthcare system by facilitating the electronic exchange of information in certain financial and administrative transactions while protecting the privacy and security of the information exchanged.

The HIPAA transaction standards are complex, and subject to differences in interpretation by third-party payors. For instance, some third-party payors may interpret the standards to require us to provide certain types of information, including demographic information not usually provided to us by physicians. As a result of inconsistent application of transaction standards by third-party payors or our inability to obtain certain billing information not usually provided to us by physicians, we could face increased costs and complexity, a temporary disruption in accounts receivable and ongoing reductions in reimbursements and net revenue. In addition, requirements for additional standard transactions, such as claims attachments or use of a national provider identifier, could prove technically difficult, time-consuming or expensive to implement, all of which could harm our business.

If we fail to comply with state and federal fraud and above laws, including anti-kickback, false claims and anti-inducement laws, we could face substantial penalties and our business, operations, and financial condition could be adversely affected.

The federal anti-kickback statute prohibits, among other things, knowingly and willfully offering, paying, soliciting or receiving remuneration to induce or in return for purchasing, leasing, ordering, or arranging for the purchase, lease or

order of any healthcare item or service reimbursable under Medicare, Medicaid, or other federal financed healthcare programs. Although there are a number of statutory exceptions and regulatory safe harbors protecting certain common activities from prosecution, the exceptions and safe harbors are drawn

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narrowly, and any remuneration to or from a prescriber or purchaser of healthcare products or services may be subject to scrutiny if they do not qualify for an exception or safe harbor. Our practices may not in all cases meet all of the criteria for safe harbor protection from anti-kickback liability.

Federal false claims laws prohibit any person from knowingly presenting or causing to be presented a false claim for payment to the federal government, or knowingly making or causing to be made a false statement to get a false claim paid. The majority of states also have statutes or regulations similar to the federal anti-kickback law and false claims laws, which apply to items or services reimbursed under Medicaid and other state programs, or, in several states, apply regardless of payor. These false claims statutes allow any person to bring suit in the name of the government alleging false and fraudulent claims presented to or paid by the government (or other violations of the statutes) and to share in any amounts paid by the entity to the government in fines or settlement. Such suits, known as qui tam actions, have increased significantly in the healthcare industry in recent years. Sanctions under these federal and state laws may include civil monetary penalties, exclusion of a manufacturer s products from reimbursement under government programs, criminal fines and imprisonment. In addition, the recently enacted Patient Protection and Affordable Care Act, among other things, amends the intent requirement of the federal anti-kickback and criminal healthcare fraud statutes. A person or entity no longer needs to have actual knowledge of this statute or specific intent to violate it. In addition, the Patient Protection and Affordable Care Act provides that the government may assert that a claim including items or services resulting from a violation of the federal anti-kickback statute constitutes a false or fraudulent claim for purposes of the false claims statutes. Because of the breadth of these laws and the narrowness of the safe harbors and exceptions, it is possible that some of our business activities could be subject to challenge under one or more of such laws. Such a challenge, regardless of the outcome, could have a material adverse effect on our business, business relationships, reputation, financial condition and results of operations.

The Patient Protection and Affordable Care Act also imposes new reporting and disclosure requirements on device and drug manufacturers for any transfer of value made or distributed to prescribers and other healthcare providers. Device and drug manufacturers will also be required to report and disclose any investment interests held by physicians and their immediate family members during the preceding calendar year. Failure to submit required information may result in civil monetary penalties of up to an aggregate of $150,000 per year (and up to an aggregate of $1 million per year for knowing failures), for all payments, transfers of value or ownership or investment interests not reported in an annual submission. As of August 1, 2013, manufacturers are required to collect data, and they will be required to submit their first data reports to the Centers for Medicare & Medicaid Services by March 31, 2014 and by the 90th day of each calendar year thereafter.

In addition, there has been a recent trend of increased federal and state regulation of payments made to physicians. Certain states, mandate implementation of compliance programs and/or the tracking and reporting of gifts, compensation and other remuneration to physicians. The shifting compliance environment and the need to build and maintain robust and expandable systems to comply with different compliance and/or reporting requirements in multiple jurisdictions increase the possibility that a healthcare company many violate one or more of the requirements.

The Federal Civil Monetary Penalties Law prohibits the offering or giving of remuneration to a Medicare or Medicaid beneficiary that the person knows or should know is likely to influence the beneficiary s selection of a particular supplier of items or services reimbursable by a Federal or state governmental program. We sometimes offer customers various discounts and other financial incentives in connection with the sales of our products. While it is our intent to comply with all applicable laws, the government may find that our marketing activities violate the Civil Monetary Penalties Law. If we are found to be in noncompliance, we could be subject to civil money penalties of up to $10,000 for each wrongful act, assessment of three times the amount claimed for each item or service and exclusion from the Federal healthcare programs.

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The scope and enforcement of each of these laws is uncertain and subject to rapid change in the current environment of healthcare reform, especially in light of the lack of applicable precedent and regulations. If our operations are found to be in violation of any of the laws described above or any other government regulations that apply to us, we may be subject to penalties, including civil and criminal penalties, damages, fines and the curtailment or restricting of our operations. Any penalties, damages, fines, curtailment or restructuring or our operations could harm our ability to operate our business and our financial results. Any action against us for violation of these laws, even if we successfully defend against it, could cause us to incur significant legal expenses and divert our management s attention from operation of our business. Moreover, achieving and sustaining compliance with applicable federal and state fraud laws may prove costly.

Foreign governments tend to impose strict price controls, which may adversely affect our future profitability.

We sell our products in 43 countries outside the United States through distributors or directly to large house accounts. In some foreign countries, particularly in the European Union, the pricing of medical devices is subject to governmental control. In these countries, pricing negotiations with governmental authorities can take considerable time after the receipt of marketing approval for a product. To obtain reimbursement or pricing approval in some countries, we may be required to supply data that compares the cost-effectiveness of our Inogen One systems to other available oxygen therapies. If reimbursement of our products is unavailable or limited in scope or amount, or if pricing is set at unsatisfactory levels, it may not be profitable to sell our products in certain foreign countries, which would negatively affect the long-term growth of our business.

Our business activities involve the use of hazardous materials, which require compliance with environmental and occupational safety laws regulating the use of such materials. If we violate these laws, we could be subject to significant fines, liabilities or other adverse consequences.

Our research and development programs as well as our manufacturing operations involve the controlled use of hazardous materials. Accordingly, we are subject to federal, state and local laws governing the use, handling and disposal of these materials. Although we believe that our safety procedures for handling and disposing of these materials comply in all material respects with the standards prescribed by state and federal regulations, we cannot completely eliminate the risk of accidental contamination or injury from these materials. In the event of an accident or failure to comply with environmental laws, we could be held liable for resulting damages, and any such liability could exceed our insurance coverage.

Risks related to our intellectual property

If we are unable to secure and maintain patent or other intellectual property protection for the intellectual property used in our products, we will lose a significant competitive advantage.

Our commercial success depends, in part, on obtaining and maintaining patent and other intellectual property protection for the technologies used in our products. The patent positions of medical device companies, including ours, can be highly uncertain and involve complex and evolving legal and factual questions. Furthermore, we might in the future opt to license intellectual property from other parties. If we, or the other parties from whom we would license intellectual property, fail to obtain and maintain adequate patent or other intellectual property protection for intellectual property used in our products, or if any protection is reduced or eliminated, others could use the intellectual property used in our products, resulting in harm to our competitive business position. In addition, patent and other intellectual property protection may not:

prevent our competitors from duplicating our products;

prevent our competitors from gaining access to our proprietary information and technology; or

permit us to gain or maintain a competitive advantage.

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Any of our patents may be challenged, invalidated, circumvented or rendered unenforceable. We cannot provide assurance that we will be successful should one or more of our patents be challenged for any reason. If our patent claims are rendered invalid or unenforceable, or narrowed in scope, the patent coverage afforded our products could be impaired, which could make our products less competitive.

As of December 31, 2013, we had six pending U.S. patent applications, 24 issued U.S. patents and one issued Canadian patent relating to the design and construction of our oxygen concentrators and our intelligent delivery technology. We cannot specify which of these patents individually or as a group will permit us to gain or maintain a competitive advantage. U.S. patents and patent applications may be subject to interference proceedings, and U.S. patents may be subject to re-examination inter partes review, post-grant review, and derivation proceedings in the U.S. Patent and Trademark Office. Foreign patents may be subject to opposition or comparable proceedings in the corresponding foreign patent offices. Any of these proceedings could result in loss of the patent or denial of the patent application, or loss or reduction in the scope of one or more of the claims of the patent or patent application. Changes in either patent laws or in interpretations of patent laws may also diminish the value of our intellectual property or narrow the scope of our protection. Interference, re-examination and opposition proceedings may be costly and time consuming, and we, or the other parties from whom we might potentially license intellectual property, may be unsuccessful in defending against such proceedings. Thus, any patents that we own or might license may provide limited or no protection against competitors. In addition, our pending patent applications and those we may file in the future may have claims narrowed during prosecution or may not result in patents being issued. Even if any of our pending or future applications are issued, they may not provide us with adequate protection or any competitive advantages. Our patents and patent applications cover particular aspects of our products. Other parties may develop and obtain patent protection for more effective technologies, designs or methods for oxygen therapy. If these developments were to occur, it would likely have an adverse effect on our sales. Our ability to develop additional patentable technology is also uncertain.

Non-payment or delay in payment of patent fees or annuities, whether intentional or unintentional, may also result in the loss of patents or patent rights important to our business. Many countries, including certain countries in Europe, have compulsory licensing laws under which a patent owner may be compelled to grant licenses to other parties. In addition, many countries limit the enforceability of patents against other parties, including government agencies or government contractors. In these countries, the patent owner may have limited remedies, which could materially diminish the value of the patent. In addition, the laws of some foreign countries do not protect intellectual property rights to the same extent as do the laws of the United States, particularly in the field of medical products and procedures

Our products could infringe the intellectual property rights of others, which may lead to patent and other intellectual property litigation that could itself be costly, could result in the payment of substantial damages or royalties, prevent us from using technology that is essential to our products, and/or force us to discontinue selling our products.

The medical device industry in general has been characterized by extensive litigation and administrative proceedings regarding patent infringement and intellectual property rights. Our competitors hold a significant number of patents relating to oxygen therapy devices and products. From time to time, we have commenced litigation to enforce our intellectual property rights. For example, we have pursued litigation against Inova Labs for infringement of two of our patents seeking damages, injunctive relief, costs, and attorneys fees. An adverse decision in this action or in any other legal action could limit our ability to assert our intellectual property rights, limit the value of our technology or otherwise negatively impact our business, financial condition and results of operations.

Monitoring unauthorized use of our intellectual property is difficult and costly. Unauthorized use of our intellectual property may have occurred or may occur in the future. Although we have taken steps to minimize the risk of this occurring, any such failure to identify unauthorized use and otherwise adequately protect our intellectual property would adversely affect our business. Moreover, if we are required to commence litigation,

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whether as a plaintiff or defendant as has occurred with Inova Labs, not only will this be time-consuming, but we will also be forced to incur significant costs and divert our attention and efforts of our employees, which could, in turn, result in lower revenue and higher expenses.

We cannot provide assurance that our products or methods do not infringe the patents or other intellectual property rights of third parties and if our business is successful, the possibility may increase that others will assert infringement claims against us.

Determining whether a product infringes a patent involves complex legal and factual issues, and the outcome of a patent litigation action is often uncertain. We have not conducted an extensive search of patents issued or assigned to other parties, including our competitors, and no assurance can be given that patents containing claims covering our products, parts of our products, technology or methods do not exist, have not been filed or could not be filed or issued. Because of the number of patents issued and patent applications filed in our technical areas, our competitors or other parties may assert that our products and the methods we employ in the use of our products are covered by U.S. or foreign patents held by them. In addition, because patent applications can take many years to issue and because publication schedules for pending applications vary by jurisdiction and some companies opt not to publish their patent applications, there may be applications now pending of which we are unaware and which may result in issued patents that our current or future products infringe. Also, because the claims of published patent applications can change between publication and patent grant, there may be published patent applications that may ultimately issue with claims that we infringe. There could also be existing patents that one or more of our products or parts may infringe and of which we are unaware. As the number of competitors in the market for oxygen products and as the number of patents issued in this area grows, the possibility of patent infringement claims against us increases. In certain situations, we may determine that it is in our best interests to voluntarily challenge a party s products or patents in litigation or other proceedings, including patent interferences or re-examinations. As a result, we may become involved in unwanted litigation that could be costly, result in diversion of management s attention, require us to pay damages and force us to discontinue selling our products.

Infringement and other intellectual property claims and proceedings brought against us, whether successful or not, could result in substantial costs and harm to our reputation. Such claims and proceedings can also distract and divert management and key personnel from other tasks important to the success of the business. We cannot be certain that we will successfully defend against allegations of infringement of patents and intellectual property rights of others. In the event that we become subject to a patent infringement or other intellectual property lawsuit and if the other party s patents or other intellectual property were upheld as valid and enforceable and we were found to infringe the other party s patents or violate the terms of a license to which we are a party, we could be required to do one or more of the following:

- cease selling or using any of our products that incorporate the asserted intellectual property, which would adversely affect our revenue;
- pay damages for past use of the asserted intellectual property, which may be substantial;
- obtain a license from the holder of the asserted intellectual property, which license may not be available on reasonable terms, if at all, and which could reduce profitability; and

redesign or rename, in the case of trademark claims, our products to avoid infringing the intellectual property rights of third parties, which may not be possible and could be costly and time-consuming if it is possible to do so.

If we are unable to prevent unauthorized use or disclosure of trade secrets, unpatented know-how and other proprietary information, our ability to compete will be harmed.

We rely on a combination of trade secrets, copyrights, trademarks, confidentiality agreements and other contractual provisions and technical security measures to protect certain aspects of our technology, especially where we do not believe that patent protection is appropriate or obtainable. We require our employees and

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consultants to execute confidentiality agreements in connection with their employment or consulting relationships with us. We also require our employees and consultants to disclose and assign to us all inventions conceived during the term of their employment or engagement while using our property or that relate to our business. We also require our corporate partners, outside scientific collaborators and sponsored researchers, advisors and others with access to our confidential information to sign confidentiality agreements. We also have taken precautions to initiate reasonable safeguards to protect our information technology systems. However, these measures may not be adequate to safeguard our proprietary intellectual property and conflicts may, nonetheless, arise regarding ownership of inventions. Such conflicts may lead to the loss or impairment of our intellectual property or to expensive litigation to defend our rights against competitors who may be better funded and have superior resources. Our employees, consultants, contractors, outside clinical collaborators and other advisors may unintentionally or willfully disclose our confidential information to competitors. In addition, confidentiality agreements may be unenforceable or may not provide an adequate remedy in the event of unauthorized disclosure. Enforcing a claim that a third party illegally obtained and is using our trade secrets is expensive and time-consuming, and the outcome is unpredictable. Moreover, our competitors may independently develop equivalent knowledge, methods and know-how. Unauthorized parties may also attempt to copy or reverse engineer certain aspects of our products that we consider proprietary, and in such cases we could not assert any trade secret rights against such party. As a result, other parties may be able to use our proprietary technology or information, and our ability to compete in the market would be harmed.

We may be subject to damages resulting from claims that our employees or we have wrongfully used or disclosed alleged trade secrets of other companies.

Many of our employees were previously employed at other medical device companies focused on the development of oxygen therapy products, including our competitors. Although no claims against us are currently pending, we may be subject to claims that these employees or we have inadvertently or otherwise used or disclosed trade secrets or other proprietary information of their former employers. Litigation may be necessary to defend against these claims. If we fail in defending such claims, in addition to paying monetary damages, we may lose valuable intellectual property rights. Even if we are successful in defending against these claims, litigation could result in substantial costs, damage to our reputation and be a distraction to management.

Risks related to being a public company

We will incur increased costs as a result of operating as a public company and our management will be required to devote substantial time to new compliance initiatives and corporate governance practices.

As a public company, and increasingly after we are no longer an emerging growth company, we will incur significant legal, accounting and other expenses that we did not incur as a private company. In addition, the Sarbanes-Oxley Act and rules subsequently implemented by the SEC and the NASDAQ Global Select Market impose numerous requirements on public companies, including establishment and maintenance of effective disclosure and financial controls and corporate governance practices. Also, the Securities Exchange Act of 1934, as amended, or the Exchange Act, requires, among other things, that we file annual, quarterly and current reports with respect to our business and operating results. Our management and other personnel will need to devote a substantial amount of time to compliance with these laws and regulations. These requirements have increased and will continue to increase our legal, accounting, and financial compliance costs and have made and will continue to make some activities more time consuming and costly. For example, we expect these rules and regulations to make it more difficult and more expensive for us to obtain director and officer liability insurance, and we may be required to incur substantial costs to maintain the same or similar coverage. These rules and regulations could also make it more difficult for us to attract and retain qualified persons to serve on our board of directors or our board committees or as executive officers.

Overall, we estimate that our incremental costs resulting from operating as a public company, including compliance with these rules and regulations, may be between $1.5 million and $3.0 million per year. However, these rules and regulations are often subject to varying interpretations, in many cases due to their lack of

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specificity, and, as a result, their application in practice may evolve over time as new guidance is provided by regulatory and governing bodies. This could result in continuing uncertainty regarding compliance matters and higher costs necessitated by ongoing revisions to disclosure and governance practices.

The Sarbanes-Oxley Act requires, among other things, that we assess the effectiveness of our internal control over financial reporting annually and the effectiveness of our disclosure controls and procedures quarterly. In particular, Section 404(a) of the Sarbanes-Oxley Act, or Section 404(a), will require us to perform system and process evaluation and testing of our internal control over financial reporting to allow management to report on the effectiveness of our internal control over financial reporting. Section 404(b) of Sarbanes-Oxley Act also requires our independent registered public accounting firm to attest to the effectiveness of our internal control over financial reporting. As an emerging growth company we expect to avail ourselves of the exemption from the requirement that our independent registered public accounting firm attest to the effectiveness of our internal control over financial reporting under Section 404(b). However, we may no longer avail ourselves of this exemption when we are no longer an emerging growth company. When our independent registered public accounting firm is required to undertake an assessment of our internal control over financial reporting, the cost of our compliance with Section 404(b) will correspondingly increase. Our compliance with applicable provisions of Section 404 will require that we incur substantial accounting expense and expend significant management time on compliance-related issues as we implement additional corporate governance practices and comply with reporting requirements.

Furthermore, investor perceptions of our company may suffer if deficiencies are found, and this could cause a decline in the market price of our stock. Irrespective of compliance with Section 404, any failure of our internal control over financial reporting could have a material adverse effect on our stated operating results and harm our reputation. If we are unable to implement these requirements effectively or efficiently, it could harm our operations, financial reporting, or financial results and could result in an adverse opinion on our internal controls from our independent registered public accounting firm.

If we fail to maintain effective internal control over financial reporting in the future, the accuracy and timing of our financial reporting may be adversely affected.

In connection with the audit of our financial statements for the years ended December 31, 2012 and 2011, we concluded that there were material weaknesses in our internal control over financial reporting. A material weakness is a significant deficiency, or a combination of significant deficiencies, in internal control over financial reporting such that it is reasonably possible that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis. The material weaknesses that we identified related to (1) a lack of sufficient staff to deal with the various rules and regulations with respect to financial reporting, (2) accounting for revenue recognition as it relates to properly recording deferred revenue, estimated earned but unbilled revenue and billing adjustments and (3) accounting for warranty revenue and cost recognition with regard to lifetime warranties.

In response to this reported material weakness, as discussed with the Audit Committee, we had undertaken in 2013 the following steps to remediate those weaknesses: (1) improved standard documentation requirements for the assessment of critical, significant and judgmental accounting matters and disclosures and financial reporting issues required by accounting principles generally accepted in the United States of America (GAAP); (2) reorganized our finance and accounting department by hiring additional qualified managers and staff for certain key positions in order to enhance oversight, review and control over financial reporting. (3) hired outside consultants with technical skills to assist in the documentation of internal controls and flows procedures. As of December 31, 2013, we believe that these corrective actions, taken as a whole, have assisted in remediating the previous material weaknesses identified.

No material weaknesses in internal control over financial reporting were identified in connection with our 2013 audit. However, our management and independent registered public accounting firm did not perform an

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evaluation of our internal control over financial reporting during any period in accordance with the provisions of the Sarbanes-Oxley Act. Had we and our independent registered public accounting firm performed an evaluation of our internal control over financial reporting in accordance with the provisions of the Sarbanes-Oxley Act, additional control deficiencies amounting to significant deficiencies or material weaknesses may have been identified. We cannot be certain as to when we will be able to implement the requirements of Section 404 of the Sarbanes-Oxley Act. If we fail to implement the requirements of Section 404 in a timely manner, we might be subject to sanctions or investigation by regulatory agencies such as the SEC. In addition, failure to comply with Section 404 or the report by us of a significant deficiency or material weakness may cause investors to lose confidence in our financial statements, and the trading price of our common stock may decline. If we fail to remedy any significant deficiency or material weakness, our financial statements may be inaccurate, our access to the capital markets may be restricted and the trading price of our ordinary shares may suffer.

We are an emerging growth company and the reduced disclosure requirements applicable to emerging growth companies may make our common stock less attractive to investors.

We are an emerging growth company, as defined in the JOBS Act, and we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced financial disclosure obligations, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, and exemptions from the requirements of holding a nonbinding advisory vote on executive compensation and any golden parachute payments not previously approved. We may take advantage of these provisions for up to five years or such earlier time that we are no longer an emerging growth company. We would cease to be an emerging growth company upon the earliest to occur of: the last day of the fiscal year in which we have more than $1.0 billion in annual revenue; the date we qualify as a large accelerated filer, with at least $700 million of equity securities held by non-affiliates; the issuance, in any three-year period, by us of more than $1.0 billion in non-convertible debt securities; and the last day of the fiscal year ending after the fifth anniversary of our initial public offering. We may choose to take advantage of some but not all of these reduced reporting burdens. If we take advantage of any of these reduced reporting burdens in future filings, the information that we provide our security holders may be different than you might get from other public companies in which you hold equity interests. We cannot predict if investors will find our common stock less attractive because we may rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile.

Risks related to our common stock

We expect that our stock price will fluctuate significantly, and you may have difficulty selling your shares.

Prior to our initial public offering, there has been no public market for shares of our common stock. We cannot predict the extent to which investor interest in our company will lead to the development of an active trading market on the NASDAQ Global Select Market or otherwise or how liquid that market might become. If an active trading market does not develop, you may have difficulty selling any of our shares of common stock that you buy. In addition, the trading price of our common stock may be highly volatile and could be subject to wide fluctuations in response to various factors, some of which are beyond our control. These factors include:

actual or anticipated quarterly variation in our results of operations or the results of our competitors;

announcements by us or our competitors of new commercial products, significant contracts, commercial relationships or capital commitments;

issuance of new or changed securities analysts reports or recommendations for our stock;

developments or disputes concerning our intellectual property or other proprietary rights;

commencement of, or our involvement in, litigation;

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market conditions in the oxygen therapy market;

reimbursement or legislative changes in the oxygen therapy market;

failure to complete significant sales;

manufacturing disruptions that could occur if we were unable to successfully expand our production in our current or an alternative facility;

any future sales of our common stock or other securities;

any major change to the composition of our board of directors or management; and

general economic conditions and slow or negative growth of our markets.

The stock market in general, and market prices for the securities of technology-based companies like ours in particular, have from time to time experienced volatility that often has been unrelated to the operating performance of the underlying companies. A certain degree of stock price volatility can be attributed to being a newly public company. These broad market and industry fluctuations may adversely affect the market price of our common stock, regardless of our operating performance. In several recent situations where the market price of a stock has been volatile, holders of that stock have instituted securities class action litigation against the company that issued the stock. If any of our stockholders were to bring a lawsuit against us, the defense and disposition of the lawsuit could be costly and divert the time and attention of our management and harm our operating results.

If securities or industry analysts do not publish research or publish unfavorable research about our business, our stock price and trading volume could decline.

The trading market for our common stock will rely in part on the research and reports that equity research analysts publish about us and our business. We will not have any control of the analysts or the content and opinions included in their reports. The price of our stock could decline if one or more equity research analysts downgrade our stock or issue other unfavorable commentary or research. If one or more equity research analysts ceases coverage of our company or fails to publish reports on us regularly, demand for our stock could decrease, which in turn could cause our stock price or trading volume to decline.

Future sales of shares could cause our stock price to decline.

If stockholders holding shares of our common stock purchased prior to our public offering sell, or indicate an intention to sell, substantial amounts of their common stock in the public market the trading price of our common stock could decline. As of February 28, 2014 we had outstanding a total of 18,147,544 shares of common stock of which only the 4,411,763 shares of common stock sold by us and the selling stockholders in our initial public offering are freely tradable, without restriction, in the public market. Each of our directors and officers, and certain of our stockholders, has entered into lock-up agreements with the underwriter of our initial public offering that restrict their ability to sell or transfer their shares. The lock-up agreements pertaining to our public offering are in effect through August 12,

2014. Our underwriters, however, may, in their sole discretion, permit our officers, directors and other current stockholders who are subject to the contractual lock-up to sell shares prior to the expiration of the lock-up agreements. After the lock-up agreements expire, based on shares outstanding as of February 28, 2014, up to an additional 13,735,781 shares of common stock will be eligible for sale in the public market, 3,013,219 of which are held by directors and executive officers and will be subject to volume limitations under Rule 144 under the Securities Act and various vesting agreements. In addition 1,571,215 shares of common stock that are issuable upon exercise of outstanding options as of February 28, 2014 will become eligible for sale in the public market to the extent permitted by the provisions of various vesting agreements, the lock-up agreements and Rules 144 and 701 under the Securities Act. If these additional shares are sold, or if it is perceived that they will be sold, in the public market, the trading price of our common stock could decline.

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Our directors, executive officers and principal stockholders will continue to have substantial control over us and could limit your ability to influence the outcome of key transactions, including changes of control.

As of March 1, 2014, our executive officers, directors and stockholders who owned more than 5% of our outstanding common stock and their respective affiliates beneficially owned or controlled approximately 69.9% of the outstanding shares of our common stock, assuming no exercise of the underwriters option to purchase additional shares which was granted by certain of our selling stockholders in connection with our initial public offering. Accordingly, these executive officers, directors and stockholders who owned more than 5% of our outstanding common stock before this offering and their respective affiliates, acting as a group, will have substantial influence over the outcome of corporate actions requiring stockholder approval, including the election of directors, any merger, consolidation or sale of all or substantially all of our assets or any other significant corporate transactions. These stockholders may also delay or prevent a change of control of us, even if such a change of control would benefit our other stockholders. The significant concentration of stock ownership may adversely affect the trading price of our common stock due to investors perception that conflicts of interest may exist or arise.

Anti-takeover provisions in our charter documents and under Delaware law could make an acquisition of us, which may be beneficial to our stockholders, more difficult and may prevent attempts by our stockholders to replace or remove our current management and limit the market price of our common stock.

Provisions in our certificate of incorporation and bylaws may have the effect of delaying or preventing a change of control or changes in our management. Our amended and restated certificate of incorporation and amended and restated bylaws include provisions that:

- authorize our board of directors to issue, without further action by the stockholders, up to 10,000,000 shares of undesignated preferred stock;
- require that any action to be taken by our stockholders be effected at a duly called annual or special meeting and not by written consent;
- specify that special meetings of our stockholders can be called only by our board of directors, the Chairman of the board of directors, or the Chief Executive Officer;
- establish an advance notice procedure for stockholder approvals to be brought before an annual meeting of our stockholders, including proposed nominations of persons for election to our board of directors;
- establish that our board of directors is divided into three classes, Class I, Class II and Class III, with each class serving staggered three year terms;
- provide that our directors may be removed only for cause;

provide that vacancies on our board of directors may be filled only by a majority of directors then in office, even though less than a quorum;

specify that no stockholder is permitted to cumulate votes at any election of directors; and

require a super-majority of votes to amend certain of the above-mentioned provisions.

These provisions may frustrate or prevent any attempts by our stockholders to replace or remove our current management by making it more difficult for stockholders to replace members of our board of directors, which is responsible for appointing the members of our management. In addition, because we are incorporated in Delaware, we are governed by the provisions of Section 203 of the Delaware General Corporation Law, which limits the ability of stockholders owning in excess of 15% of our outstanding voting stock to merge or combine with us.

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We have broad discretion in the use of the net proceeds from our initial public offering and may not use them effectively.

We have broad discretion in the application of the net proceeds from our initial public offering and could spend the proceeds in ways that do not improve our results of operations or enhance the value of our common stock. We intend to use approximately $15 million of the net proceeds from our initial public offering for investments in rental assets; approximately $5 million of the net proceeds for sales and marketing activities, including expansion of our sales force to support the ongoing commercialization of our products; approximately $3 million of the net proceeds for research and product development activities; approximately $11 million of the net proceeds for facilities improvements or expansions and the purchase of manufacturing and other equipment; and the remainder of the net proceeds for working capital and other general corporate purposes. We may also use a portion of our net proceeds to acquire and invest in complementary products, technologies or businesses; however, we currently have no agreements or commitments to complete any such transaction. We have not allocated these net proceeds for any specific purposes. We might not be able to yield a significant return, if any, on any investment of these net proceeds. Stockholders will not have the opportunity to influence our management s decisions on how to use the net proceeds, and our failure to apply these funds effectively could have a material adverse effect on our business and cause the price of our common stock to decline.

We have never paid dividends on our capital stock, and we do not anticipate paying any cash dividends in the foreseeable future.

We have paid no cash dividends on any of our classes of capital stock to date, have contractual restrictions against paying cash dividends and currently intend to retain our future earnings to fund the development and growth of our business. As a result, capital appreciation, if any, of our common stock will be your sole source of gain for the foreseeable future.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

We lease approximately 39,000 square feet of manufacturing and office space at our corporate headquarters in Goleta, California under a lease that expires in September 2015, and approximately 31,000 square feet of manufacturing and office space in Richardson, Texas under a lease that expires in December 2019. In addition, we lease office space in Smyrna, Tennessee, and Corinth, Mississippi under leases expiring in August 2014 and May 2014, respectively. We believe that our existing facilities are adequate to meet our business requirements for the near-term and that additional space will be available on commercially reasonable terms, if required.

ITEM 3. LEGAL PROCEEDINGS

On November 4, 2011, we 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. We alleged in the Lawsuit that certain of Defendant s oxygen concentrators infringe various claims of the 343 and 136 patents. The Lawsuit seeks damages, injunctive relief, costs and attorney fees.

The Defendant has answered the complaint, denying infringement and asserting various sets of defenses including non-infringement, invalidity and unenforceability, patent misuse, unclean hands, laches and estoppel. The Defendant also filed counterclaims against us alleging patent invalidity, non-infringement and inequitable

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conduct. We denied the allegations in the Defendant s counterclaims. We have 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 other legal proceedings arising in the normal course of business. The Company carries insurance, subject to deductibles under the specified policies, to protect against losses from certain types of legal claims. The Company does not anticipate that any of these proceedings will have a material impact on the Company.

ITEM 4. MINE SAFETY DISCLOSURES

None.

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PART II

ITEM 5. MARKET FOR REGISTRANT S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information and Holders

Our common stock has been publicly traded on the NASDAQ Global Select Market under the symbol INGN since February 14, 2014. Prior to that time, there was no public market for our common stock. As a result, we have not set forth quarterly information with respect to the high and low prices for our common stock for the two most recent fiscal years.

On February 28, 2014, the closing price for our common stock as reported on the NASDAQ Global Select Market was $17.51 per share.

Dividend Policy

We have never declared or paid any cash dividends on our common stock or any other securities. We anticipate that we will retain all available funds and any future earnings, if any, for use in the operation of our business and do not anticipate paying cash dividends in the foreseeable future. In addition, our revolving credit and term loan agreement materially restricts, and future debt instruments we issue may materially restrict, our ability to pay dividends on our common stock. Payment of future cash dividends, if any, will be at the discretion of our board of directors after taking into account various factors, including our financial condition, operating results, current and anticipated cash needs, the requirements of current or then-existing debt instruments and other factors our board of directors deems relevant.

Stockholders

As of March 13, 2014, there were 84 registered stockholders of record for our common stock. The actual number of stockholders is greater than this number of record holders and includes stockholders who are beneficial owners but whose shares are held in street name by brokers and other nominees. This number of holders of record also does not include stockholders whose shares may be held in trust by other entities.

Equity Compensation Plan Information

The following table summarizes the number of outstanding options, warrants and rights granted to our employees, consultants, and directors, as well as the number of shares of common stock remaining available for future issuance, under our equity compensation plans as of December 31, 2013.

	Number of Securities to be Issued Upon Exercise of Outstanding Options (a)	Weighted Average Exercise Price of Outstanding Options and Rights (b)	Reserved for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column(a))

Equity compensation plans approved by security holders				
2002 Stock Incentive Plan (1)	1,384,062	$	1.11	
2012 Equity Incentive Plan (2)	944,613	$	3.15	276,839
2014 Equity Incentive Plan (3)				
Equity compensation plans not approved by security holders				
Total	2,328,675	$	1.94	276,839

(1) The 2002 Stock Incentive Plan was terminated in March 2012 in connection with the adoption of our Equity Incentive Plan and, accordingly, no shares were available for issuance under this plan after that time. The 2002 Stock Incentive Plan continues to govern outstanding stock options granted thereunder.

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(2) The 2012 Equity Incentive Plan terminated in connection with the initial public offering of our common stock in February of 2014 and was replaced by the 2014 Equity Incentive Plan. Accordingly, no shares were available for issuance under this plan after that time.
(3) The 2014 Equity Incentive Plan was approved by the board and stockholders on October 11, 2013, but did not become effective until immediately prior to the effectiveness of our Registration Statement in connection with our Initial Public Offering in February 2014. Accordingly, no shares were outstanding or available for issuance on December 31, 2013.

Stock Performance Graph

The stock performance graph required by Section 201(e) of Regulation S-K has been omitted as our common stock was not publicly traded during any portion of the period described in Section 201(e).

Use of Proceeds from Initial Public Offering of Common Stock

On February 12, 2014, our Registration Statement on Form S-1, as amended (Reg. No. 333- 192605) was declared effective in connection with the IPO of our common stock, pursuant to which we sold 3,529,411 shares at a price to the public of $16.00 per share. Additionally, the selling stockholders sold 981,902 shares of common stock (882,352 upon the IPO, and 99,550 of which were sold pursuant to a 30-day option granted to the underwriters). The offering closed on February 20, 2014, as a result of which we received net proceeds of approximately $52.5 million after underwriting discounts of approximately $3.9 million, but before offering expenses of approximately $2.4 million. We did not receive any proceeds from the shares sold by the selling stockholders. J.P. Morgan acted as sole book-running manager for the offering, Leerink Partners acted as lead manager, and William Blair and Stifel acted as co-managers. No payments for such expenses were made directly or indirectly to (i) any of our officers or directors or their associates, (ii) any persons owning 10% or more of any class of our equity securities, or (iii) any of our affiliates.

There has been no material change in the planned use of proceeds from our initial public offering as described in our final prospectus filed with the SEC pursuant to Rule 424(b) under the Securities Act of 1933, as amended, on February 14, 2014.

Recent Sales of Unregistered Securities

The following list sets forth information regarding all unregistered securities sold by us since January 1, 2013. No underwriters were involved in the sales and the certificates representing the securities sold and issued contain legends restricting transfer of the securities without registration under the Securities Act or an applicable exemption from registration.

(a) From January 1, 2013 through December 31, 2013, we granted to certain of our employees, consultants, directors and other service providers under our 2012 Equity Incentive Plan options to purchase an aggregate of 716,326 shares of our common stock at exercise prices ranging from $1.17 to $8.37 per share.

(b) From January 1, 2013 through December 31, 2013, we issued and sold an aggregate of 8,874 shares of our common stock upon the exercise of options issued to certain employees, directors and consultants under our 2002 Stock Incentive Plan at exercise prices ranging from $0.60 to $8.70, for aggregate consideration of approximately $11,965.

(c) On February 14, 2013, we issued 19,976 shares of our series D convertible preferred stock upon exercise of warrants at an exercise price of $21.90 per share for aggregate proceeds of approximately $437,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 37,543 shares of common stock.

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(d) On February 28, 2013, we issued 19,539 shares of our series D convertible preferred upon exercise of warrants at an exercise price of $21.90 per share for aggregate proceeds of approximately $428,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 36,722 shares of common stock.

(e) On May 20, 2013, we issued 7,989 shares of our series D convertible preferred stock upon exercise of warrants at an exercise price of $21.90 per share for aggregate proceeds of approximately $175,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 15,014 shares of common stock.

(f) On May 23, 2013, we issued 2,951 shares of our series D convertible preferred stock upon exercise of a warrant at an exercise price of $21.90 per share for aggregate proceeds of approximately $65,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 5,546 shares of common stock.

(g) On June 21, 2013, we issued 5,706 shares of our series D convertible preferred stock upon exercise of warrants at an exercise price of $21.90 per share for aggregate proceeds of approximately $125,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 10,724 shares of common stock.

(h) On July 3, 2013, we issued 3,685 shares of our series D convertible preferred stock upon exercise of a warrant at an exercise price of $21.90 per share for aggregate proceeds of approximately $81,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 6,925 shares of common stock.

(i) On August 28, 2013, we issued 22,830 shares of our series D convertible preferred stock upon exercise of warrants at an exercise price of $21.90 per share for aggregate proceeds of approximately $500,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 42,907 shares of common stock.

(j) On September 5, 2013, we issued 2,853 shares of our series D convertible preferred stock upon exercise of a warrant at an exercise price of $21.90 per share for aggregate proceeds of approximately $62,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 5,362 shares of common stock.

(k) On October 28, 2013, we issued 372 shares of our series D convertible preferred stock upon exercise of a warrant at an exercise price of $21.90 per share for aggregate proceeds of approximately $8,000. Upon completion of our initial public offering on February 20, 2014 these shares converted to approximately 699 shares of common stock.

Unless otherwise indicated, the offers, sales and issuances of the securities described in Items (c) through (k) were exempt from registration under the Securities Act under Section 4(2) of the Securities Act as transactions by an issuer

not involving a public offering. The recipients of securities in each of these transactions acquired the securities for investment only and not with a view to or for sale in connection with any distribution thereof and appropriate legends were affixed to the securities issued in these transactions. Each of the recipients of securities in these transactions was an accredited person and had adequate access, through employment, business or other relationships, to information about the registrant. No underwriters were involved in the offers, sales and issuances of the securities described in items (c) through (k).

The offers, sales and issuances of the securities described in Items (a) through (b) were exempt from registration under the Section 4(2) of the Securities Act and/or Rule 701 of the Securities Act.

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ITEM 6. SELECTED FINANCIAL DATA

The following selected historical financial data should be read in conjunction with Part II, Item 7, Management s Discussion and Analysis of Financial Condition and Results of Operations , our financial statements and the related notes included in Item 8, Financial Statements and Supplementary Data of this Annual Report on Form 10-K.

The statements of operations data for the years ended December 31, 2013, 2012 and 2011 and the balance sheet data as of December 31, 2013 and 2012 are derived from our audited financial statements included in Part II, Item 8, Financial Statements and Supplementary Data in this Annual Report on Form 10-K. The balance sheet data as of December 31, 2011 is derived from our audited financial statements not included in this Annual Report on Form 10-K. Our historical results are not necessarily indicative of the results that may be expected in the future and our interim results are not necessarily indicative of results to be expected for the full fiscal year.

(amounts in thousands, except share and per share amounts)	**Year ended December 31, 2013**	**2012**	**2011**
Statements of operations data:			
Revenue			
Sales revenue	$ 43,971	$ 28,077	$ 19,076
Rental revenue	30,538	19,872	10,977
Sales of used rental equipment	200	95	46
Other revenue	734	532	535
Total revenue	75,443	48,576	30,634
Cost of revenue			
Cost of sales revenue	24,209	17,359	12,127
Cost of rental revenue	12,146	7,243	3,783
Cost of used rental equipment sales	97	25	20
Total cost of revenue	36,452	24,627	15,930
Gross profit	38,991	23,949	14,704
Operating expenses:			
Research and development	2,398	2,262	1,789
Sales and marketing	18,375	12,569	9,014
General and administrative	13,754	8,289	5,623
Total operating expenses	34,527	23,120	16,426
Income (loss) from operations	4,464	829	(1,722)
Other expense, net	(616)	(247)	(267)
Income (loss) before provision (benefit) for income taxes	3,848	582	(1,989)
Provision (benefit) for income taxes	(21,587)	18	13

Net income (loss)	25,435	564	(2,002)
Less deemed dividend on redeemable convertible preferred stock	(7,278)	(5,781)	(3,027)
Net income (loss) after deemed dividend	18,157	(5,217)	(5,029)
Less preferred rights dividend	(7,165)		
Less undistributed earnings to preferred stock	(10,781)		
Net income (loss) attributable to common stockholders	$ 211	$ (5,217)	$ (5,029)

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Years ended December 31,	2013	2012	2011
Numerator basic and diluted:			
Net income (loss)	$ 25,435	$ 564	$ (2,002)
Less deemed dividend on redeemable preferred stock	(7,278)	(5,781)	(3,027)
Net income (loss) after deemed dividend	18,157	(5,217)	(5,029)
Less preferred rights dividend	(7,165)		
Less: undistributed earnings to preferred stock	(10,781)		
Net income (loss) attributable to common stockholders	$ 211	$ (5,217)	$ (5,029)
Numerator diluted			
Net income (loss)	$ 25,435	$ 564	$ (2,002)
Less deemed dividend on redeemable preferred stock	(7,278)	(5,781)	(3,027)
Net income (loss) after deemed dividend	18,157	(5,217)	(5,029)
Less preferred rights dividend	(7,165)		
Less: undistributed earnings to preferred stock	(9,625)		
	$ 1,367	$ (5,217)	$ (5,029)
Denominator:			
Weighted-average common shares basic common stock	276,535	261,268	249,519
Weighted-average common shares diluted common stock	2,008,156	261,268	249,519
Net income (loss) per share basic common stock	$ 0.76	$ (19.97)	$ (20.15)
Net income per share diluted common stock	$ 0.68	$	$
Shares excluded from diluted income (loss)			
Common stock warrants		233,611	250,997
Preferred convertible stock		14,057,509	10,899,820
Stock options		1,646,223	1,425,624
Shares excluded from diluted income (loss)		15,937,343	12,576,441

(1) See note 2 to each of our audited financial statements included elsewhere in this Annual Report on Form 10-K for an explanation of the calculations of our basic and diluted net loss per share attributable to common stockholders and pro forma net loss per share attributable to common stockholders.

(2) For a discussion of our use of EBITDA, Adjusted EBITDA and Adjusted net income and their calculations, please see Non GAAP financial measures.

	Year ended December 31,		
(amounts in thousands)	**2013**	**2012**	**2011**
Balance sheet data:			
Cash and cash equivalents	$ 13,521	$ 15,112	$ 3,906
Working capital	13,159	12,880	1,302
Total assets	82,397	47,586	24,131
Total indebtedness	10,649	8,936	9,629
Deferred revenue	1,487	1,094	594
Total liabilities	26,098	19,011	16,575
Redeemable convertible preferred stock	118,671	109,345	83,122
Total stockholders deficit	62,372	80,770	75,566

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Non-GAAP financial measures

EBITDA, Adjusted EBITDA, and Adjusted net income (loss) are a financial measures that are not calculated in accordance with generally accepted accounting principles in the United States, or GAAP. We define EBITDA as net income or loss excluding interest income, interest expense, taxes and depreciation and amortization. Adjusted EBITDA also excludes the change in the fair value of our preferred stock warrant liability and stock-based compensation. Below, we have provided a reconciliation of EBITDA, Adjusted EBITDA, and Adjusted net income (loss) to our net income or loss, the most directly comparable financial measure calculated and presented in accordance with GAAP. EBITDA, Adjusted EBITDA, and Adjusted net income (loss) should not be considered alternatives to net income or loss or any other measure of financial performance calculated and presented in accordance with GAAP. Our EBITDA, and Adjusted EBITDA, and Adjusted net income (loss) may not be comparable to similarly titled measures of other organizations because other organizations may not calculate EBITDA, Adjusted EBITDA, and Adjusted net income (loss) in the same manner as we calculate these measures.

We include EBITDA, Adjusted EBITDA and Adjusted net income (loss) in this 10-K because they are important measures upon which our management assesses our operating performance. We use EBITDA, Adjusted EBITDA and Adjusted net income (loss) as key performance measures because we believe they facilitate operating performance comparisons from period to period by excluding potential differences primarily caused by variations in capital structures, tax positions, the impact of depreciation and amortization expense on our fixed assets, changes related to the fair value re-measurements of our preferred stock warrant, and the impact of stock-based compensation expense. Because EBITDA, Adjusted EBITDA and Adjusted net income (loss) facilitate internal comparisons of our historical operating performance on a more consistent basis, we also use EBITDA, Adjusted EBITDA and Adjusted net income (loss) for business planning purposes, to incentivize and compensate our management personnel, and in evaluating acquisition opportunities. In addition, we believe EBITDA, Adjusted EBITDA and Adjusted net income (loss) and similar measures are widely used by investors, securities analysts, ratings agencies, and other parties in evaluating companies in our industry as a measure of financial performance and debt-service capabilities.

Our use of EBITDA, Adjusted EBITDA and Adjusted net income (loss) have limitations as analytical tools, and you should not consider them in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

- EBITDA, Adjusted EBITDA and Adjusted net income (loss) do not reflect our cash expenditures for capital equipment or other contractual commitments;
- Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and EBITDA, Adjusted EBITDA and Adjusted net income (loss) do not reflect capital expenditure requirements for such replacements;
- EBITDA, Adjusted EBITDA and Adjusted net income (loss) do not reflect changes in, or cash requirements for, our working capital needs;
- EBITDA, Adjusted EBITDA, and Adjusted net income (loss) do not reflect the interest expense or the cash requirements necessary to service interest or principal payments on our indebtedness; and

Other companies, including companies in our industry, may calculate EBITDA, Adjusted EBITDA and Adjusted net income (loss) measures differently, which reduces their usefulness as a comparative measure. In evaluating EBITDA, Adjusted EBITDA, and Adjusted net income (loss) you should be aware that in the future we will incur expenses similar to the adjustments in this presentation. Our presentation of EBITDA, Adjusted EBITDA and Adjusted net income (loss) should not be construed as an inference that our future results will be unaffected by these expenses or any unusual or non-recurring items. When evaluating our performance, you should consider EBITDA, Adjusted EBITDA and Adjusted net income (loss) alongside other financial performance measures, including our net loss and other GAAP results.

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The following table presents a reconciliation of EBITDA and Adjusted EBITDA to our net income or loss, the most comparable GAAP measure, for each of the periods indicated:

EBITDA and Adjusted EBITDA	Year ended December 31,		
(in thousands)	**2013**	**2012**	**2011**
Net income (loss)	$ 25,435	$ 564	$ (2,002)
Non-GAAP adjustments:			
Interest income	(12)	(88)	(113)
Interest expense	562	493	261
Provision (benefit) for income taxes	(21,587)	18	13
Depreciation and amortization	8,544	4,984	3,198
EBITDA	12,942	5,971	1,357
Change in fair value of preferred stock warrant liability	262	(148)	119
Stock-based compensation	230	60	144
Adjusted EBITDA	$ 13,434	$ 5,883	$ 1,620
Net income (loss) (GAAP)	$ 25,435	$ 564	$ (2,002)
Non-GAAP			
One-time benefit from reversal of deferred tax valuation adjustment	(21,807)		
Adjusted net income (loss)	$ 3,628	$ 564	$ (2,002)

	Years ended December 31,	
	2013	**2012**
Non-GAAP pro-forma results of EPS calculation(1)(2)		
Numerator basic and diluted:		
Net income	$ 25,435	$ 564
Less deemed dividend on redeemable preferred stock		
Net income attributable to common stockholders	$ 25,435	$ 564
Net income per share basic common stock	$ 1.74	$ 0.04
Net income per share diluted common stock	$ 1.55	$ 0.04
Denominator:		
Weighted-average common shares basic common stock	14,636,950	14,601,861
Weighted-average common shares diluted preferred stock	16,368,571	15,486,487

The pro forma EPS calculations gives effect to: (1) the automatic conversion of the outstanding convertible preferred stock into a weighted average of 14,219,001 and 14,216,838 shares of common stock, for the years ended December 31, 2013 and 2012, respectively. (2) the cash exercise of warrants to purchase an aggregate of 142,495 shares of common stock, which we expect will occur prior to closing of the IPO as the warrants will otherwise expire at that time and (3) the reclassification of our preferred stock warrant liability to additional paid-in-capital upon the closing of the IPO.

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ITEM 7. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of the financial condition and results of our operations should be read in conjunction with the financial statements and related notes included elsewhere in this report. This discussion contains forward-looking statements that involve risks and uncertainties. Our actual results could differ materially from those discussed below. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled Risk Factors included elsewhere in this report.

Item 7. ***Management s Discussion and Analysis of Financial Condition and Results of Operation.***

You should read the following discussion and analysis of our financial condition and results of operations together with the financial statements and the related notes thereto included elsewhere in this 10-K. This discussion contains forward-looking statements that reflect our plans, estimates and beliefs. Our actual results may differ materially from those discussed in these forward-looking statements. Factors that could cause or contribute to these differences include those discussed below and elsewhere in this Annual Report on Form 10-K, particularly in the section of the 10-K entitled Risk factors and Forward -looking statements.

Overview

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

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

We believe our direct-to-consumer strategy has been critical to driving patient adoption of our technology. All other portable oxygen concentrator manufacturers access patients through home medical equipment providers, which we

believe are disincentivized to encourage portable oxygen concentrator adoption. In order to facilitate the regular delivery and pickup of oxygen tanks, home medical equipment providers have invested in geographically dispersed distribution infrastructures consisting of delivery vehicles, physical locations, and

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delivery personnel within each area. Because portable oxygen concentrator technology eliminates the need for physical distribution infrastructure but has higher initial equipment costs than oxygen tanks and cylinders, we believe converting to a portable oxygen concentrator model would require both significant restructuring and capital investment for home medical equipment providers. Our direct-to-consumer marketing strategy allows us to sidestep the home medical equipment channel, appeal to patients directly, and capture both the manufacturing and provider margin. We believe our ability to capture this top-to-bottom margin, combined with our portable oxygen concentrator technology that eliminates the need for the costs associated with oxygen deliveries, gives us a cost structure advantage over our competitors using the delivery model.

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

Expand our sales and marketing channels. We will continue to hire additional internal sales representatives to drive our direct-to-consumer marketing efforts. During the year ended December 31, 2013, we increased our internal sales force from 93 to 108. Additionally, we are building a physician referral channel that currently consists of eleven employees. Lastly, we are focused on building our international distribution capabilities.

Invest in our product offerings to develop innovative products. We expended $2.4 million, $2.3 million and $1.8 million in 2013, 2012 and 2011, respectively, in research and development expenses, and we intend to continue to make such investments in the foreseeable future.

Secure contracts with healthcare payors and insurers. Based on our patient population, we estimate that at least 30% of oxygen therapy patients are covered by non-Medicare payors, and that these patients often represent a younger, more active patient segment. By becoming an in-network provider with more insurance companies, we can reduce the co-insurance for patients, which we believe will allow us to attract additional patients to our Inogen One solutions.

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

Historically, we have generated a majority of our revenue from sales and rentals to customers in the United States. In 2013, 2012 and 2011, approximately 22%, 27% and 26%, respectively, of our total revenue was from customers outside the United States, primarily in Europe. To date, all of our revenue has been denominated in United States dollars. We sell our products in 43 countries outside the United States through distributors or directly to large house accounts, which include gas companies and home oxygen providers. In this case, we sell to and bill the distributor or house accounts directly, leaving responsibility for the patient billing, support and clinical setup to the local provider. As of January 1, 2014, we had four employees who focused on selling our products to distributors and house accounts outside the United States.

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Our total revenue increased $26.8 million to $75.4 million in 2013 from $48.6 million in 2012, due to growth in rental revenue associated with an increase in the number of patients using Medicare or private payors to rent our products, and growth in sales revenue associated with the increases in international sales and direct-to-consumer cash sales of our Inogen One systems and new product launches. We generated Adjusted EBITDA of $13.4 million and $5.9 million in 2013 and 2012, respectively. Adjusted net income was $3.6 million before the one-time benefit from the reversal of deferred tax valuation for 2013, compared to adjusted net income of $0.6 million for 2012. We generated net income of $25.4 million in 2013 and net income of $0.6 million in 2012. As of December 31, 2013, our accumulated deficit was $62.6 million.

The vast majority of our revenue consists of sales revenue and rental revenue.

Sales revenue

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

Our direct-to-consumer sales process involves numerous interactions with the individual patient, the physician and the physician s staff, and includes an in-depth analysis and review of our product, the patient s diagnosis and prescribed oxygen therapy, including procuring an oxygen prescription, and assessing the patient s available insurance benefits. The patient may consider whether to finance the product through an Inogen-approved third party or whether to purchase the equipment. Product is not deployed until both the prescription and payment are received. Once product is deployed, the patient has 30 days to return the product under a trial, subject to the patient payment of a minimal processing and handling fee. Approximately 5% to 10% of patients who purchase a system for cash return the system during this 30-day trial period. As a result, we have experienced fluctuations in our direct-to-consumer sales on a period-to-period basis in the past, a trend that we anticipate will continue in the future.

Our business-to-business efforts are focused on selling to home medical equipment distributors, oxygen providers and resellers who are based inside and outside of the United States. This process involves interactions with various key customer stakeholders, including sales, purchasing, product testing, and clinical personnel. Businesses that have patient demand that can be met with our portable oxygen concentrator systems place purchase orders to secure product deployment. This may be influenced based on outside factors, including the result of tender offerings, changes in insurance plan coverage, and overall changes in the net oxygen therapy patient population. Products are shipped FOB Inogen, and based on financial history and profile, businesses may either prepay or receive extended terms. As a result of these factors, product purchases can be subject to changes in demand by customers. Given the potential for variability in ordering history that we have in the past experienced, and likely will in the future experience, there may be fluctuations in our business-to-business sales on a period-to-period basis.

We sold approximately 19,200 Inogen One systems in 2013, approximately 11,900 Inogen One systems in 2012 and approximately 7,300 in 2011. Management focuses on system sales as an indicator of current business success.

Rental revenue

Our rental process involves numerous interactions with the individual patient, the physician and the physician s staff. The process includes an in-depth analysis and review of our product, the patient s diagnosis and oxygen needs, and their medical history to confirm the appropriateness of our product for the patient s oxygen therapy and compliance with Medicare and private payor billing requirements, which often necessitates additional physician evaluation and/or testing as well as a Certificate of Medical Necessity. Once the product is

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deployed, the patient receives direction on product use and receives a clinical titration from our licensed staff to confirm the product meets the patient s needs prior to billing. As a result, the time from initial contact with a customer to billing can vary significantly and be up to one month or longer.

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

As the rental patient base increases, this rental model generates recurring revenue with minimal additional sales and general and administrative expenses. A portion of rentals include a capped rental period when no additional reimbursement will be allowed unless additional criteria are met. In this scenario, the ratio of billable patients to patients on service is critical to maintaining rental revenue growth as patients on service increases. As the rental base expands, we expect our rental revenue to increase and over time to become an increasingly important contributor to our total revenue. Over time, we believe that our rental revenue should be subject to less period-to-period fluctuation than our sales revenue.

As of December 31, 2013, we had over 21,300 oxygen rental patients, an increase from over 13,500 oxygen rental patients as of December 31, 2012 and approximately 7,500 in 2011. Management focuses on rental revenue as an indicator of current business success and a leading indicator of likely future rental revenue; however, actual rental revenue recognized is subject to a variety of other factors, including reimbursement levels by patient zip code, the number of capped patients, and adjustments for patients in transition.

Reimbursement

We rely heavily on reimbursement from Medicare, and secondarily from private payors and Medicaid, for our rental revenue. For the year ended December 31, 2013, approximately 58% of our rental revenue was derived from Medicare. The U.S. list price for our stationary oxygen rentals (E1390) is $260 per month and for our oxygen generating portable equipment (OGPE) rentals (E1392) is $70 per month. The current standard Medicare allowable effective January 1, 2014 for stationary oxygen rentals (E1390) is $178.24 per month and for OGPE rentals (E1392) is $51.63 per month. These are the two primary codes that we bill to Medicare and other payors for our product rentals.

As of January 1, 2011, Medicare has phased in a program called competitive bidding. Competitive bidding impacts the amount Medicare pays suppliers of durable medical equipment, including portable oxygen concentrators. The program is defined geographically, with suppliers submitting bids to provide medical equipment for a specific product category within that geography. Once bids have been placed, an individual company s bids across products within the category are aggregated and weighted by each product s market share in the category. The weighted average price is then indexed against competitors. Medicare determines a clearing price out of these weighted average prices at which sufficient suppliers have indicated they will support patients in the category, and this threshold is typically designed to generate theoretical supply that is twice the expected demand. Bids for each modality among the suppliers that made the cut are then arrayed to determine what Medicare will reimburse for each product category. The program has strict anti-collusion guidelines to ensure bidding is truly competitive. Competitive bidding contracts last three years once implemented, after which they are subject to a new round of bidding. Discounts off the standard Medicare allowable occur in competitive bidding Metropolitan Statistical Areas where contracts have been awarded as well as in cases

where private payors pay less than this allowable. Current Medicare payment rates in competitive bidding areas are at 48-64% of the standard Medicare allowable for stationary oxygen rentals (average of $93.29 per month) and OGPE rentals are at 70-92% of the standard Medicare allowable (average of $42.33 per month). Competitive bidding

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rates are based on the zip code where the patient resides. Rental revenue includes payments for product, disposables, and customer service/support. Medicare has not announced specific plans for the plan to implement competitive bidding nationwide, but by 2016 Medicare must implement competitive bidding or competitive bidding pricing for included items to non-competitive bidding areas. In February 2014, Medicare solicited public comment on the methodology it would use to comply with statue.

The following table sets forth the current Medicare standard allowable reimbursement rates and the weighted average reimbursement rates applicable in Metropolitan Statistical Areas covered by rounds one and two of competitive bidding. The round one re-compete was completed in the same Metropolitan Statistical Areas as round one for the next three year period starting 1/1/14 when the original contracts expire.

	Medicare standard allowable effective 1/1/14	**Round one weighted average 1/1/11-12/11/13**	**Round two weighted average 7/1/13-6/30/16**	**Round one re-compete weighted average 1/1/14-12/31/16**
E1390	$ 178.24	$ 116.16	$ 93.07	$ 95.74
E1392	51.63	41.89	42.72	38.08
Total	$ 229.87	$ 158.05	$ 135.79	$ 133.82
% of standard		*69%*	*59%*	*58%*

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

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

Following round one of competitive bidding, we were excluded from the Kansas City-MO-KS, Miami-Fort Lauderdale-Pompano-FL, and Orlando Kissimmee-FL competitive bidding areas and Honolulu-Hawaii, where we have never maintained a license. After round one recompete, we gained access to Kansas City-MO-KS and were excluded from the following competitive bidding areas: Cleveland-Elyria-Mentor-OH, Cincinnati-Middletown-OH, Miami-Fort Lauderdale-Pompano-FL, Orlando Kissimmee-FL, Pittsburg-PA, Riverside-San Bernardino-Ontario-CA. After round two of competitive bidding, we were excluded from an additional 10 competitive bidding areas, including Akron-OH, Cape Coral-Fort Myers-FL, Deltona-Daytona Beach-Ormond Beach-FL, Jacksonville-FL, Lakeland-Winter Haven-FL, North Port-Bradenton-Sarasota-FL, Ocala, Palm Bay-Melbourne-Titusville-FL, Tampa-St. Petersburg-Clearwater-FL and Toledo-OH. Collectively, we have incrementally lost access to approximately seven percent of the Medicare market. As a result, on a going forward basis we will continue to have

access to approximately 90% of the Medicare market based on our analysis of the 92 competitive bidding areas that we have won out of the 109 competitive bidding areas, representing 59% of the market, with the remaining 41% of the market not subject to competitive bidding. The incremental loss of access to approximately seven percent of the Medicare market is expected to have an adverse impact on our rental business, which represented approximately 41% of our total revenue in the year ended December 31, 2013. However, we expect the decline in total revenue resulting from the loss of competitive bidding contract in the areas that we were excluded from to be partially offset by the grandfathering of existing Medicare patients and direct sales to former Medicare patients with third party insurance coverage or who

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pay cash. Our revenue from Medicare in the 17 competitive bidding areas where we were not offered contracts was approximately $1.7 million in 2013 and $1.0 million in 2012.

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

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

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

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

In addition to the adoption of the competitive bidding program, reimbursable fees for oxygen rental services in non-competitive bidding areas were eligible to receive mandatory annual Consumer Price Index for all Urban Consumers, or CPI-U, updates beginning in 2010. The CPI-U for 2012 was +3.6%, but the multi-factor productivity adjustment remained -1.2%, so the net result was a 2.4% increase in fee schedule payments in 2012 for items and services not included in an area subject to competitive bidding. For 2013, the CPI-U is +1.7%, but the adjustment is -0.9%, so the net result is a 0.8% increase in fee schedule payments in 2013. For 2014, the CPI-U is +1.8%, but the adjustment is -0.8%, so the net result is a 1.0% increase in fee schedule payments in 2014. However, the stationary oxygen equipment codes payment amounts, as required by statute, must be adjusted on an annual basis, as necessary, to ensure budget neutrality of the new payment class for oxygen generating portable equipment. Thus, the increase in allowable payment amounts for stationary oxygen equipment codes increased 0.5% from 2013 to 2014. At this time, it is unclear if the current CPI-U method or a proposed inflation method included in President Obama s 2014 fiscal

budget proposal would apply to future year s calculations.

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As of December 31, 2013, we had 44 contracts with Medicaid and private payors. These contracts qualify us an in-network provider for these payors. As a result, patients can use our systems at the same cost as other in-network oxygen therapy solutions, including those utilizing the delivery model. Based on our patient population, we believe at least 30% of all oxygen therapy patients are covered by private payors. Private payors typically provide reimbursement at 60% to 100% of Medicare allowables for in-network plans, and private payor plans can have 36-month caps similar to Medicare. We anticipate that private payor reimbursement levels will generally be reset in accordance with Medicare payment amounts established through competitive bidding.

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

Basis of presentation

The following describes the line items set forth in our statements of operations.

Revenue

We classify our revenue in four main categories: sales revenue, rental revenue, sale of used rental equipment and other revenue. There will be fluctuations in mix between business-to-business sales, direct-to-consumer sales and rentals from period to period. We expect rental revenue should constitute a larger percentage of total revenue, which would increase our gross margins. In addition, we expect both the average selling price and the manufacturing cost of our products to decrease following the introduction of future generations of our Inogen One systems. Inogen One system selling prices and gross margins for our Inogen One systems may fluctuate as we introduce new products and reduce our product costs. For example, the gross margin for our Inogen One G3 is higher than our Inogen One G2. Thus, to the extent our sales of our Inogen One G3 systems are higher than sales of our Inogen One G2 systems, our overall gross margins should improve and, conversely, to the extent our sales of our Inogen One G2 systems are higher than sales of our Inogen One G3 systems, our overall gross margins should decline.

Sales revenue. Our sales revenue is derived from the sale of our Inogen One systems and related accessories to patients in the United States and to home healthcare providers, distributors and resellers worldwide. Sales revenue is classified into two areas: business-to-business sales and direct-to-consumer sales. For the years ended December 31, 2013, 2012 and 2011, business-to-business sales as a percentage of sales revenue were 60%, 68% and 67%, respectively. Generally, our direct-to-consumer sales have higher margins than our business-to-business sales.

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

Sales of used rental equipment. Our sales of used rental equipment revenue is derived from the sale of our Inogen One systems and related accessories to home healthcare providers and patients when the product has previously been sold

or rented to another patient or business. Sales in this category are not material.

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Other revenue. Other revenue consists of service and freight revenue. Revenue from the sales of our services is recognized when no significant obligations remain undelivered and collection of the receivables is reasonably assured. We offer extended service contracts on our 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.

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

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

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

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

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

Cost of revenue

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

production volume and yields.

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Operating expenses

Research and development

Research and development expenses consist primarily of personnel-related expenses, including salaries, benefits and stock-based compensation, allocated facility costs, laboratory supplies, consulting fees and related costs, costs associated with patent amortization costs, patent legal fees including defense costs and testing costs for new product launches. We have made substantial investments in research and development since our inception. Our research and development efforts have focused primarily on the tasks required to enhance our technologies and to support development and commercialization of new and existing products. We expect to have moderate increases in research and development expense over time.

Sales and marketing

Our sales and marketing expenses primarily support our direct-to-consumer strategy. Our sales and marketing expenses consist primarily of personnel-related expenses, including salaries, commissions, benefits, and stock-based compensation, for employees, and allocated facilities costs. They also include expenses for media and advertising, informational kits, public relations and other promotional and marketing activities, including travel and entertainment expenses, as well as customer service and clinical services. Sales and marketing expenses increased throughout 2013 primarily due to an increase in the sales force and the increasing number of rental patients and we expect a further increase in 2014 as we continue to increase sales and marketing activities.

General and administrative

General and administrative expenses consist primarily of personnel-related expenses, including salaries, benefits, and stock-based compensation for employees in our compliance, finance, medical billing, human resources, information technology, business development and general management functions, and allocated facilities costs. In addition, general and administrative expenses include professional services, such as legal, consulting and accounting services. We expect general and administrative expenses to increase in future periods as the number of administrative personnel grows and we continue to introduce new products, broaden our customer base and grow our business. We also expect legal, accounting and compliance costs to increase due to costs associated with our initial public offering and with being a public company.

Other income (expense), net

Other income (expense), net consists primarily of interest expense related to our revolving credit and term loan agreement and interest income driven by the interest accruing on cash and cash equivalents and on past due customer balances. Other income (expense) also includes the change in valuation of warrant liability based on the Monte Carlo valuation model.

Result of operations

Comparison of years ended December 31, 2013 and 2012

Revenue

(dollars in thousands)	Year ended December 31, 2013	2012	Change 2013 vs. 2012 $	%
Revenue:				
Sales revenue	$ 43,971	$ 28,077	$ 15,894	56.6%
Rental revenue	30,538	19,872	10,666	53.7%
Sales of used equipment	200	95	105	110.5%
Other revenue	734	532	202	38.0%
Total revenue	$ 75,443	$ 48,576	$ 26,867	55.3%

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The increase in sales revenue in the year ended December 31, 2013 compared to the year ended December 31, 2012 was attributable to an increase in the number of systems sold primarily related to the launch of the Inogen One G3, an increase in direct-to-consumer sales in the United States due to increased sales and marketing efforts, and an increase in business-to-business sales worldwide as the adoption of portable oxygen concentrators improved.

The increase in rental revenue in the year ended December 31, 2013 compared to the year ended December 31, 2012 was attributable to the increase in rental patients from over 13,500 as of December 31, 2012 to over 21,300 as of December 31, 2013 due to additional marketing efforts and increased sales personnel. This increase was partially offset by the reduced reimbursement rates resulting from round two competitive bidding that became effective in 91 Metropolitan Statistical Areas on July 1, 2013. As expected, the growth in sales revenue was not impacted by the reduced reimbursement rates resulting from competitive bidding. Sales revenue grew 56.6% for the year ended December 31, 2013 compared to previous year-over-year growth of 47.2%.

Cost of revenue and gross profit

	Year ended December 31,		Change 2013 vs. 2012	
(dollars in thousands)	**2013**	**2012**	**$**	**%**
Cost of sales revenue	$ 24,209	$ 17,359	$ 6,850	39.5%
Cost of rental revenue	12,146	7,243	4,903	67.7%
Cost of used rental equipment sales	97	25	72	288.0%
Total cost of revenue	$ 36,452	$ 24,627	$ 11,825	48.0%
Gross profit	38,991	23,949	15,042	62.8%
Gross margin %	51.7%	49.3%		

We manufacture our Inogen One product line in our Goleta, California and Richardson, Texas facilities. Our manufacturing process includes final assembly, testing, and packaging to customer specifications. The increase in cost of sales revenue was attributable to an increase in the number of systems sold, partially offset by reduced bill of material and labor and overhead costs for our products associated with better sourcing and increased volumes. The increase in cost of rental revenue was attributable to an increase of rental patients and related rental assets, depreciation and product exchange and logistics costs. Cost of rental revenue includes depreciation of our rental assets of $7.1 million for year ended December 31, 2013 versus $4.1 million for the year ended December 31, 2012.

Gross margin is defined as revenue less costs of revenue divided by revenue. The overall increase in sales and rental revenue, the increase in sales and rental revenue with respect to our higher margin Inogen One G3 as compared to our Inogen One G2, and the continued shift towards direct-to-consumer sales revenue in our revenue mix, partially offset by declining rental reimbursement rates, account for the gross margin improvement from 49.3% to 51.7% in the year ended December 31, 2012 and 2013, respectively. The increase is primarily due to the increase in sales mix toward direct-to-consumer from provider sales. The rental revenue gross margin was 60% in the year ended December 31, 2013 versus 64% in the year ended December 31, 2012 due to lower rental reimbursement rates resulting from round two Competitive Bidding that became effective July 1, 2013, partially offset by lower asset deployment costs per patient and also additional economies of scale of our servicing costs. The sales revenue gross margin was 45% in the year ended December 31, 2013 versus 39% in the year ended December 31, 2012 was primarily due to the reduction in average cost per unit sold and improved sales revenue mix towards direct-to-consumer sales.

Research and development expense

	2.40		0.0%			
Total/Average	9	804,078	$ 2.55	$ 2.55	$ 0.0%	$

(1) Leasing spreads on a gross rent basis (base rent plus common area maintenance, real estate taxes, and other charges) were (5.6%) for New Leases - Previously Leased Space and (6.0%) for Renewals.
(2) Leasing spreads on a gross rent basis were 2.2% for New Leases - Previously Leased Space and (2.3%) for Renewals.
(3) These leasing costs are presented as annualized costs per square foot and are spread uniformly over the initial lease term.
(4) This category includes newly constructed and recommissioned space.
(5) This category includes expansions, relocations and lease extensions.

As of June 30, 2011, for non-anchor leases, the average minimum rent per square foot as of the expiration date was $21.05 for the renewing leases in Holdover status, $27.54 for the remaining leases expiring in 2011 and $23.64 for leases expiring in 2012.

Real Estate Revenue

Real estate revenue decreased by $0.3 million, or 0%, in the three months ended June 30, 2011 compared to the three months ended June 30, 2010, primarily due to:

A decrease of $0.8 million in expense reimbursements. At many of our malls, we have continued to recover a lower proportion of common area maintenance and real estate tax expenses. Our properties continue to experience a trend towards more gross leases (leases that provide that tenants pay a higher minimum rent in

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lieu of contributing toward common area maintenance costs and real estate taxes), as well as more leases that provide for the rent amount to be determined on the basis of a percentage of sales in lieu of minimum rent or any contribution toward common area maintenance or real estate tax expenses. In recent years, we have entered into agreements with some tenants experiencing financial difficulties to convert their leases to gross leases or percentage of sales leases, resulting in lower expense reimbursements.

A decrease of $0.1 million in base rents, including a $0.6 million net decrease in straight line rent resulting from write-offs associated with the Borders Group, Inc. planned liquidation. This decrease was offset by base rent increases of $0.4 million at Cherry Hill Mall and $0.3 million at Woodland Mall due to new store openings; and

An increase of $0.3 million in lease termination revenue as a result of $0.6 million received from one tenant during the three months ended June 30, 2011.

Real estate revenue decreased by $2.5 million, or 1%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010, primarily due to:

A decrease of $1.5 million in lease termination revenue as a result of $1.7 million received from four tenants during 2010 that did not recur; and

A decrease of $1.3 million in expense reimbursements for the reasons discussed above.

Operating Expenses

Operating expenses were unchanged in the three months ended June 30, 2011 compared to the three months ended June 30, 2010, as increases in common area maintenance expenses were offset by a decrease in bad debt expense.

Operating expenses increased by $0.5 million, or 0%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010, primarily due to:

An increase of $0.7 million in common area maintenance expenses as a result of stipulated annual contractual increases in housekeeping and security services;

An increase of $0.3 million in real estate tax expense; and

A decrease of $0.6 million in non-common area utility expense, including a $1.0 million decrease at seven of our Pennsylvania properties where electric rates have decreased as a result of deregulation and alternate supplier contracts executed over the past 12 months.

Net Operating Income (NOI)

NOI (a non-GAAP measure) is derived from real estate revenue (determined in accordance with generally accepted accounting principles, or GAAP, including lease termination revenue) minus operating expenses (determined in accordance with GAAP), plus our share of revenue and operating expenses of our partnership investments as described below, and includes real estate revenue and operating expenses from properties included in discontinued operations. It does not represent cash generated from operating activities in accordance with GAAP and should not be considered to be an alternative to net income (determined in accordance with GAAP) as an indication of our financial performance or to be an alternative to cash flow from operating activities (determined in accordance with GAAP) as a measure of our liquidity. It is not indicative of funds available for our cash needs, including our ability to make cash distributions. We believe that NOI is helpful to management and investors as a measure of operating performance because it is an indicator of the return on property investment, and provides a method of comparing property performance over time. We believe that net income is the most directly comparable GAAP measurement to NOI.

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NOI excludes interest and other income, general and administrative expenses, interest expense, depreciation and amortization, gains on sales of interests in real estate, gains or sales of non-operating real estate, gains on sales of discontinued operations, gain on extinguishment of debt, impairment losses, project costs and other expenses.

The following tables present NOI for the three and six months ended June 30, 2011 and 2010. The results are presented using the proportionate-consolidation method (a non-GAAP measure), which presents our share of the results of our partnership investments. Under GAAP, we account for our partnership investments under the equity method of accounting. Operating results for retail properties that we owned for the full periods presented (Same Store) exclude properties acquired or disposed of during the periods presented. A reconciliation of NOI to net loss calculated in accordance with GAAP appears under the heading Reconciliation of GAAP Net Loss to Non-GAAP Measures.

	Same Store Three months ended June 30,			Non Same Store Three months ended June 30,			Total Three months ended June 30,		
(in thousands of dollars)	2011	2010	% Change	2011	2010	% Change	2011	2010	% Change
Real estate revenue	$ 116,166	$ 116,971	(1%)	$ 470	$ 3,681	(87%)	$ 116,636	$ 120,652	(3%)
Operating expenses	(49,884)	(49,939)	0%	(465)	(1,005)	(54%)	(50,349)	(50,944)	(1%)
Net Operating Income	$ 66,282	$ 67,032	(1%)	$ 5	$ 2,676	(100%)	$ 66,287	$ 69,708	(5%)

	Same Store Six months ended June 30,			Non Same Store Six months ended June 30,			Total Six months ended June 30,		
(in thousands of dollars)	2011	2010	% Change	2011	2010	% Change	2011	2010	% Change
Real estate revenue	$ 234,543	$ 237,412	(1%)	$ 954	$ 7,401	(87%)	$ 235,497	$ 244,813	(4%)
Operating expenses	(101,498)	(101,335)	0%	(951)	(2,141)	(56%)	(102,449)	(103,476)	(1%)
Net Operating Income	$ 133,045	$ 136,077	(2%)	$ 3	$ 5,260	(100%)	$ 133,048	$ 141,337	(6%)

Total NOI decreased by $3.4 million, or 5%, in the three months ended June 30, 2011 compared to the three months ended June 30, 2010, including a decrease of $2.7 million relating to Non Same Store properties, which resulted primarily from the sale of five power centers in 2010, and $0.6 million relating to a write off of straight line rent in connection with the planned liquidation of Borders Group, Inc. See Discontinued Operations below for further information. Same Store NOI decreased by $0.7 million. See Real Estate Revenue and Operating Expenses above for further information about our consolidated properties.

Total NOI decreased by $8.3 million, or 6%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010, including a decrease of $5.3 million relating to Non Same Store properties, which resulted primarily from the sale of five power centers in 2010, and $0.9 million relating to a write off of straight line rent in connection with the bankruptcy filing and planned liquidation of Borders Group, Inc. See Discontinued Operations below for further information. Same Store NOI decreased by $3.0 million. See Real Estate Revenue and Operating Expenses above for further information about our consolidated properties.

NOI includes lease termination revenue of $0.7 million and $0.6 million for the three months ended June 30, 2011 and 2010, respectively, and $0.7 million and $2.5 million for the six months ended June 30, 2011 and 2010, respectively.

Depreciation and Amortization

Depreciation and amortization expense decreased by $3.7 million, or 9%, in the three months ended June 30, 2011 compared to the three months ended June 30, 2010, primarily due to:

A decrease of $5.9 million because certain lease intangibles and tenant improvements at 28 properties purchased during 2003 became fully amortized in 2010; and

An increase of $2.2 million due to a higher asset base resulting from capital improvements at our properties, particularly at properties where we have completed redevelopments that have been placed in

service, and $1.0 million resulting from tenant improvement and deferred leasing commission write-offs associated with tenant bankruptcies.

Depreciation and amortization expense decreased by $9.9 million, or 12%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010, primarily due to:

A decrease of $12.6 million because certain lease intangibles and tenant improvements at 28 properties purchased during 2003 became fully amortized in 2010; and

An increase of $2.8 million, including $1.7 million resulting from tenant improvement and deferred leasing commission write-offs associated with tenant bankruptcies, due to a higher asset base resulting from capital improvements at our properties, particularly at properties where we have completed redevelopments that have been placed in service.

General and Administrative Expenses

General and administrative expenses increased by $0.8 million, or 8%, in the three months ended June 30, 2011 compared to the three months ended June 30, 2010. The increase is primarily due to a $1.1 million increase in compensation costs, which was driven by increases in incentive compensation expense, salaries and benefit costs.

General and administrative expenses increased by $0.7 million, or 4%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010. The increase is primarily due to a $1.6 million increase in compensation costs, offset by a $0.3 million reduction in professional fees and a $0.6 million decrease in other miscellaneous expenses.

Interest Expense

Interest expense decreased by $3.1 million, or 8%, in the three months ended June 30, 2011 compared to the three months ended June 30, 2010. Of this amount, $2.3 million of the decrease was due to a reduction of deferred financing costs recorded in May 2010 in connection with a partial repayment of the 2010 Term Loan that did not recur in 2011. The remaining decrease was primarily due to a lower overall debt balance and lower applicable stated interest rates, partially offset by decreased capitalized interest after assets were placed in service. Our weighted average borrowing rate was 6.41% for the three months ended June 30, 2011 compared to 6.56% for the three months ended June 30, 2010.

Interest expense decreased by $3.6 million, or 5%, in the six months ended June 30, 2011 compared to the six months ended June 30, 2010. Of this amount, $2.3 million of the decrease was due to a reduction of deferred financing costs recorded in May 2010 in connection with a partial repayment of the 2010 Term Loan that did not recur in 2011. The remaining decrease was primarily due to a lower overall debt balance, partially offset by higher applicable stated interest rates and decreased capitalized interest after assets were placed in service. Our weighted average borrowing rate was 6.26% for the six months ended June 30, 2011 compared to 6.00% for the six months ended June 30, 2010.

Equity in Income of Partnerships

Equity in income of partnerships decreased by $1.8 million, or 61%, for the three months ended June 30, 2011 compared to the three months ended June 30, 2010. The decrease was primarily due to an increase in mortgage interest expense of the partnerships of $1.0 million, a decrease in revenue of $0.5 million and an increase in other expenses of $0.3 million.

Equity in income of partnerships decreased by $2.3 million, or 47%, for the six months ended June 30, 2011 compared to the six months ended June 30, 2010. The decrease was primarily due to an increase in mortgage interest expense of the partnerships of $2.2 million and a decrease in revenue of $0.2 million, partially offset by a decrease in other expenses of $0.1 million.

Gains on Sales of Real Estate

Gains on sales of interests in real estate were $1.4 million in the three and six months ended June 30, 2011 due to a $0.7 million gain from the sale of a parcel and related land improvements at Pitney Road Plaza in Lancaster, Pennsylvania and a $0.7 million gain from the sale of condominium interest in the mall at Voorhees Town Center, in Voorhees, New Jersey.

There were no gains on sales of real estate in the three or six months ended June 30, 2010.

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Discontinued Operations

We have presented as discontinued operations the operating results of the five power centers that were sold in 2010: Creekview Center, Monroe Marketplace, New River Valley Center, Pitney Road Plaza and Sunrise Plaza.

Operating results for properties included in discontinued operations for the three months and six months ended June 30, 2010 were as follows (there was no income from discontinued operations in the three and six months ended June 30, 2011):

(in thousands of dollars)	Three months ended June 30, 2010	Six months ended June 30, 2010
Operating results of:		
Creekview Center	$ (85)	$ (182)
Monroe Marketplace	292	540
New River Valley Center	67	123
Pitney Road Plaza	138	270
Sunrise Plaza	188	370
Income from discontinued operations	$ 600	$ 1,121

Funds From Operations

The National Association of Real Estate Investment Trusts (NAREIT) defines Funds From Operations (FFO), which is a non-GAAP measure commonly used by REITs, as income before gains and losses on sales of operating properties and extraordinary items (computed in accordance with GAAP); plus real estate depreciation; plus or minus adjustments for unconsolidated partnerships to reflect funds from operations on the same basis.

We use FFO and FFO per diluted share and unit of limited partnership interest in our operating partnership (OP Unit) in measuring our performance against our peers and as one performance measure for determining incentive compensation amounts earned under certain of our performance-based executive compensation programs. We compute FFO in accordance with standards established by NAREIT, which may not be comparable to FFO reported by other REITs that do not define the term in accordance with the current NAREIT definition, or that interpret the current NAREIT definition differently than we do.

FFO does not include gains and losses on sales of operating real estate assets, which are included in the determination of net income in accordance with GAAP. Accordingly, FFO is not a comprehensive measure of our operating cash flows. In addition, since FFO does not include depreciation on real estate assets, FFO may not be a useful performance measure when comparing our operating performance to that of other non-real estate commercial enterprises. We compensate for these limitations by using FFO in conjunction with other GAAP financial performance measures, such as net income and net cash provided by operating activities, and other non-GAAP financial performance measures, such as NOI. FFO does not represent cash generated from operating activities in accordance with GAAP and should not be considered to be an alternative to net income (determined in accordance with GAAP) as an indication of our financial performance or to be an alternative to cash flow from operating activities (determined in accordance with GAAP) as a measure of our liquidity, nor is it indicative of funds available for our cash needs, including our ability to make cash distributions. We believe that net income is the most directly comparable GAAP measurement to FFO.

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The following table presents FFO for the three months ended June 30, 2011 and 2010:

(in thousands, except per share amounts)	Three months ended June 30, 2011	Three Months Ended June 30, 2010
Funds from operations	$ 18,999	$ 19,672
Accelerated amortization of deferred financing costs	100	2,258
Impairment of assets	225	
Funds from operations, as adjusted	$ 19,324	$ 21,930
Funds from operations per diluted share and OP Unit	$ 0.33	$ 0.37
Accelerated amortization of deferred financing costs	0.00	0.04
Impairment of assets	0.00	0.00
Funds from operations per diluted share and OP Unit, as adjusted	$ 0.33	$ 0.41
Weighted average number of shares outstanding	54,680	50,317
Weighted average effect of full conversion of OP Units	2,329	2,329
Effect of common share equivalents	851	587
Total weighted average shares outstanding, including OP Units	57,860	53,233

The following table presents FFO for the six months ended June 30, 2011 and 2010:

(in thousands, except per share amounts)	Six months ended June 30, 2011	Six months ended June 30, 2010
Funds from operations	$ 40,308	$ 45,196
Accelerated amortization of deferred financing costs	100	2,258
Impairment of assets	225	
Funds from operations, as adjusted	$ 40,633	$ 47,454
Funds from operations per diluted share and OP Unit	$ 0.70	$ 0.91
Accelerated amortization of deferred financing costs	0.00	0.05
Impairment of assets	0.00	
Funds from operations per diluted share and OP Unit, as adjusted	$ 0.70	$ 0.95
Weighted average number of shares outstanding	54,567	47,013
Weighted average effect of full conversion of OP Units	2,329	2,329
Effect of common share equivalents	922	349
Total weighted average shares outstanding, including OP Units	57,818	49,691

FFO was $19.0 million for the three months ended June 30, 2011, a decrease of $0.7 million, or 3%, compared to FFO of $19.7 million for the three months ended June 30, 2010. This decrease was primarily due to:

the sale of five power centers in 2010; and

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a decrease in Same Store NOI.

FFO per diluted share and OP Unit decreased $0.04 per share to $0.33 per share for the three months ended June 30, 2011, compared to $0.37 per share for the three months ended June 30, 2010.

FFO was $40.3 million for the six months ended June 30, 2011, a decrease of $4.9 million, or 11%, compared to FFO of $45.2 million for the six months ended June 30, 2010. This decrease was primarily due to:

the sale of five power centers in 2010; and

a decrease in Same Store NOI, including a $1.7 million decrease in lease termination revenue.

FFO per diluted share and OP Unit decreased $0.21 per share to $0.70 per share for the six months ended June 30, 2011, compared to $0.91 per share for the six months ended June 30, 2010.

Reconciliation of GAAP Net Loss to Non-GAAP Measures

The preceding discussions compare our unaudited Consolidated Statements of Operations results for different periods determined in accordance with GAAP. Also, the non-GAAP measures of NOI and FFO are discussed. We believe that NOI is helpful to management and investors as a measure of operating performance because it is an indicator of the return on property investment, and provides a method of comparing property performance over time. We believe that FFO is helpful to management and investors as a measure of operating performance because it excludes gains on sales of operating real estate and depreciation and amortization of real estate, among other items. FFO is a commonly used measure of operating performance and profitability among REITs, and we use FFO and FFO per diluted share and OP Unit as supplemental non-GAAP measures to compare our performance for different periods to that of our industry peers.

The following information is provided to reconcile NOI and FFO, which are non-GAAP measures, to net loss, a GAAP measure:

	Three months ended June 30, 2011			
(in thousands of dollars)	**Consolidated**	**Share of unconsolidated partnerships**	**Discontinued operations**	**Total**
Real estate revenue	$ 107,391	$ 9,245	$	$ 116,636
Operating expenses	(47,467)	(2,882)		(50,349)
Net operating income	**59,924**	**6,363**		**66,287**
General and administrative expenses	(10,433)			(10,433)
Interest and other income	809			809
Project costs and other expenses	(353)			(353)
Interest expense, net	(34,941)	(2,858)		(37,799)
Gains on sales of non operating real estate	710			710
Depreciation on non real estate assets	(222)			(222)
Funds from operations	**15,494**	**3,505**		**18,999**
Gains on sales of real estate	740			740
Depreciation on real estate assets	(36,392)	(2,358)		(38,750)
Equity in income of partnerships	1,147	(1,147)		
Net loss	**$ (19,011)**	**$**	**$**	**$ (19,011)**

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(in thousands of dollars)	Three months ended June 30, 2010 Consolidated	Share of unconsolidated partnerships	Discontinued operations	Total
Real estate revenue	$ 107,700	$ 9,797	$ 3,155	$ 120,652
Operating expenses	(47,446)	(2,894)	(604)	(50,944)
Net operating income	**60,254**	**6,903**	**2,551**	**69,708**
General and administrative expenses	(9,617)			(9,617)
Interest and other income	598			598
Project costs and other expenses	(161)			(161)
Interest expense, net	(37,998)	(1,853)	(627)	(40,478)
Depreciation on non real estate assets	(378)			(378)
Funds from operations	**12,698**	**5,050**	**1,924**	**19,672**
Depreciation on real estate assets	(39,896)	(2,102)	(1,324)	(43,322)
Equity in income of partnerships	2,948	(2,948)		
Income from discontinued operations	600		(600)	
Net loss	**$ (23,650)**	**$**	**$**	**$ (23,650)**

(in thousands of dollars)	Six months ended June 30, 2011 Consolidated	Share of unconsolidated partnerships	Discontinued operations	Total
Real estate revenue	$ 216,953	$ 18,544	$	$ 235,497
Operating expenses	(96,560)	(5,889)		(102,449)
Net operating income	**120,393**	**12,655**		**133,048**
General and administrative expenses	(20,015)			(20,015)
Interest and other income	1,727			1,727
Project costs and other expenses	(497)			(497)
Interest expense, net	(68,554)	(5,637)		(74,191)
Gains on sales of non operating real estate	710			710
Depreciation on non real estate assets	(474)			(474)
Funds from operations	**33,290**	**7,018**		**40,308**
Gains on sale of real estate	740			740
Depreciation on real estate assets	(70,650)	(4,328)		(74,978)
Equity in income of partnerships	2,690	(2,690)		
Net loss	**$ (33,930)**	**$**	**$**	**$ (33,930)**

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(in thousands of dollars)	Six months ended June 30, 2010 Consolidated	Share of unconsolidated partnerships	Discontinued operations	Total
Real estate revenue	$ 219,430	$ 19,035	$ 6,348	$ 244,813
Operating expenses	(96,103)	(5,999)	(1,374)	(103,476)
Net operating income	**123,327**	**13,036**	**4,974**	**141,337**
General and administrative expenses	(19,303)			(19,303)
Interest and other income	1,326			1,326
Project costs and other expenses	(455)			(455)
Interest expense, net	(72,204)	(3,437)	(1,252)	(76,893)
Depreciation on non real estate assets	(816)			(816)
Funds from operations	**31,875**	**9,599**	**3,722**	**45,196**
Depreciation on real estate assets	(80,188)	(4,561)	(2,601)	(87,350)
Equity in income of partnerships	5,038	(5,038)		
Income from discontinued operations	1,121		(1,121)	
Net loss	**$ (42,154)**	**$**	**$**	**$ (42,154)**

LIQUIDITY AND CAPITAL RESOURCES

This Liquidity and Capital Resources section contains certain forward-looking statements that relate to expectations and projections that are not historical facts. These forward-looking statements reflect our current views about our future liquidity and capital resources, and are subject to risks and uncertainties that might cause our actual liquidity and capital resources to differ materially from the forward-looking statements. Additional factors that might affect our liquidity and capital resources include those discussed in the section entitled Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 31, 2010 filed with the Securities and Exchange Commission. We do not intend to update or revise any forward-looking statements about our liquidity and capital resources to reflect new information, future events or otherwise.

Capital Resources

We expect to meet our short-term liquidity requirements, including distributions to shareholders, recurring capital expenditures, tenant improvements and leasing commissions, but excluding development and redevelopment projects, generally through our available working capital and net cash provided by operations, and subject to the terms and conditions of our 2010 Credit Facility. We believe that our net cash provided by operations will be sufficient to allow us to make any distributions necessary to enable us to continue to qualify as a REIT under the Internal Revenue Code of 1986, as amended. The aggregate distributions made to common shareholders and OP Unitholders in the six months ended June 30, 2011 were $17.4 million, based on distributions of $0.30 per share and OP Unit. The following are some of the factors that could affect our cash flows and require the funding of future cash distributions, recurring capital expenditures, tenant improvements or leasing commissions with sources other than operating cash flows:

- adverse changes or prolonged downturns in general, local or retail industry economic, financial, credit or capital market or competitive conditions, leading to a reduction in real estate revenue or cash flows or an increase in expenses;
- deterioration in our tenants business operations and financial stability, including tenant bankruptcies, leasing delays or terminations, or lower sales, causing deferrals or declines in rent, percentage rent and cash flows;
- inability to achieve targets for, or decreases in, property occupancy and rental rates, resulting in lower or delayed real estate revenue and operating income;

increases in operating costs that cannot be passed on to tenants, resulting in reduced operating income and cash flows; and

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increases in interest rates resulting in higher borrowing costs.

We expect to meet certain of our longer term requirements, such as remaining obligations to fund development and redevelopment projects and certain capital requirements, including scheduled debt maturities, future property and portfolio acquisitions, expenses associated with acquisitions and renovations, expansions and other non-recurring capital improvements, through a variety of capital sources, subject to the terms and conditions of our 2010 Credit Facility.

The conditions in the market for debt capital and commercial mortgage loans, including the commercial mortgage backed securities market, and the conditions in the economy and their effect on retail sales, as well as our significant leverage resulting from debt incurred to fund our redevelopment program and other development activity, have combined to necessitate that we vary our approach to obtaining, using and recycling capital. We intend to consider all of our available options for accessing the capital markets, given our position and constraints.

In the past, one avenue available to us to finance our obligations or new business initiatives has been to obtain unsecured debt, based in part on the existence of properties in our portfolio that were not subject to mortgage loans. The terms of the 2010 Credit Facility include our grant of a security interest consisting of a first lien on 20 properties. As a result, we have very few remaining assets that we could use to support unsecured debt financing. Our lack of properties in the portfolio that could be used to support unsecured debt might limit our ability to obtain capital in this way.

We are contemplating ways to reduce our leverage through a variety of means available to us, and subject to and in accordance with the terms and conditions of the 2010 Credit Facility. These steps might include obtaining equity capital, including through the issuance of equity securities if market conditions are favorable, through joint ventures or other partnerships or arrangements involving our contribution of assets with institutional investors, private equity investors or other REITs, through sales of properties with values in excess of their mortgage loans or allocable debt and application of the excess proceeds to debt reduction, or through other actions.

In March 2009, the SEC declared effective our $1.0 billion universal shelf registration statement. In May 2010, we issued 10,350,000 common shares in a public offering at $16.25 per share. We received net proceeds from the offering of approximately $160.6 million. We used the net proceeds from this offering, plus available working capital, to repay borrowings under our 2010 Credit Facility. Currently, we may use the remaining availability under our shelf registration statement to offer and sell common shares of beneficial interest, preferred shares and various types of debt securities, among other types of securities, to the public. However, we may be unable to issue securities under the shelf registration statement, or otherwise, on terms that are favorable to us, or at all.

Amended, Restated and Consolidated Senior Secured Credit Agreement

In March 2010, we entered into the 2010 Credit Facility (as defined below), which consisted of a revolving line of credit with an original capacity of $150.0 million (the Revolving Facility) and term loans with an original aggregate balance of $520.0 million and a balance prior to the amendment described below of $340.0 million (collectively, the 2010 Term Loan and, together with the Revolving Facility, and as amended as described below, the 2010 Credit Facility).

In June 2011, we amended our 2010 Credit Facility, whereby the capacity of the Revolving Facility was increased by $100.0 million to $250.0 million and we repaid $100.0 million of the 2010 Term Loan with proceeds from the Revolving Facility, after which the 2010 Term Loan had a balance of $240.0 million. The amendment also extended the term of the 2010 Credit Facility by one year to March 10, 2014 and eliminated the mandatory pay down requirements from capital events, among other changes.

The amendment lowered the interest rate range to between 2.75% and 4.00% per annum over LIBOR, depending on our leverage. Previously, the interest rate range was between 4.00% and 4.90% per annum over LIBOR. Initially, the new rate in effect is 4.00% per annum over LIBOR.

The amendment also modifies several of the financial covenants under the 2010 Credit Facility. The maximum permitted leverage ratio has been reduced to 70% from 75%, and the Corporate Debt Yield, as defined, is required to be at least 9.50% until March 30, 2012, then at least 9.75% for the next year, and at least 10.00% after March 31, 2013. The maximum amount that may be borrowed under the 2010 Credit Facility is subject to a minimum facility debt yield of 9.75%, based on the net operating income of our collateral properties. The range of applicable stated interest rates may be further reduced at our option to between 2.00% and 3.00% per annum over LIBOR, we will have an option to extend the maturity date of the 2010 Credit Facility by one year to March 10, 2015, and we may increase the maximum amount available under the Revolving Facility from $250.0 million to $350.0 million, if commitments can be obtained, and provided that the minimum facility debt yield will be increased to 11.00%, under specified conditions and subject to certain financial covenants.

In addition to the covenants described above, the 2010 Credit Facility contains affirmative and negative covenants of the type customarily found in credit facilities of this nature. As of June 30, 2011, we were in compliance with all of these covenants.

As of June 30, 2011, $70.0 million was outstanding under our Revolving Facility. We pledged $0.6 million as collateral for letters of credit, and the unused portion that was available to us was $179.4 million at June 30, 2011. In July 2011, we repaid $25.0 million of the outstanding amount under the Revolving Facility. After this paydown, the outstanding amount under the Revolving Facility was $45.0 million, $0.6 million was pledged as collateral for letters of credit and the unused portion that was available to us was $204.4 million.

The weighted average interest rate on outstanding Revolving Facility borrowings as of June 30, 2011 was 4.19%. Interest expense related to the Revolving Facility was $0.6 million and $0.5 million for the three months ended June 30, 2011 and 2010, respectively, and $0.7 million and $0.8 million for the six months ended June 30, 2011 and 2010, respectively, excluding non-cash amortization of deferred financing fees.

As of June 30, 2011, $240.0 million was outstanding under the 2010 Term Loan. The weighted average effective interest rates based on amounts borrowed under the 2010 Term Loan for the three and six months ended June 30, 2011 were 5.85% and 5.89%, respectively. Interest expense related to the 2010 Term Loan was $5.6 million and $6.5 million, respectively, for the three months ended June 30, 2011 and 2010, and $10.7 million and $8.3 million, respectively, for the six months ended June 30, 2011 and 2010, excluding non-cash amortization of deferred financing fees.

Deferred financing fee amortization associated with the 2010 Credit Facility for the three months ended June 30, 2011 and 2010 was $1.0 million and $3.4 million, respectively. Deferred financing fee amortization associated with the 2010 Credit Facility for the six months ended June 30, 2011 and 2010 was $1.9 million and $3.7 million, respectively.

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Exchangeable Notes

As of June 30, 2011 and December 31, 2010, $136.9 million in aggregate principal amount of our 4.0% Senior Exchangeable Notes due 2012 (the Exchangeable Notes) remained outstanding, excluding debt discount of $1.8 million and $2.8 million, respectively.

Interest expense related to our Exchangeable Notes for each of the three months ended June 30, 2011 and 2010 was $1.4 million, excluding the non-cash amortization of debt discount of $0.5 million and the non-cash amortization of deferred financing fees of $0.2 million. Interest expense was $2.7 million for each of the six months ended June 30, 2011 and 2010 excluding the non-cash amortization of debt discount of $1.0 million and $0.9 million, respectively, and the non-cash amortization of deferred financing fees of $0.4 million and $0.3 million for the six months ended June 30, 2011 and June 30, 2010, respectively. The Exchangeable Notes have an effective interest rate of 5.90%.

Interest Rate Derivative Agreements

As of June 30, 2011, we had entered into 10 interest rate swap agreements and one interest rate cap agreement that have a weighted average interest rate of 2.65% (excluding the spread on the related debt) on a notional amount of $687.5 million maturing on various dates through November 2013, and one forward starting interest rate swap agreement that has an interest rate of 2.96% (excluding the spread on the related debt) on a notional amount of $200.0 million maturing in March 2013.

We entered into these interest rate swap agreements (including the forward starting swap agreements) and cap agreement in order to hedge the interest payments associated with our LIBOR based debt. We have assessed the effectiveness of these interest rate swap agreements and cap agreement as hedges at inception and on a quarterly basis. On June 30, 2011, we considered these interest rate swap agreements and the cap agreement to be highly effective as cash flow hedges. The interest rate swap agreements and cap agreement are net settled monthly.

As of June 30, 2011, the aggregate estimated unrealized net loss attributed to these interest rate derivatives was $25.5 million. The carrying amount of the derivative assets is reflected in Deferred costs and other assets, the associated liabilities are reflected in Accrued expenses and other liabilities and the net unrealized loss is reflected in Accumulated other comprehensive loss in the accompanying balance sheets.

As of June 30, 2011, the fair value of derivatives in a net liability position, which excludes accrued interest but includes any adjustment for nonperformance risk related to these agreements, was $25.5 million. If we had breached any of the default provisions in these agreements as of June 30, 2011, we might have been required to settle our obligations under the agreements at their termination value (including accrued interest) of $28.2 million. We had not breached any of the provisions as of June 30, 2011.

Mortgage Loan Activity

In June 2011, the unconsolidated partnership that owns Red Rose Commons in Lancaster, Pennsylvania entered into a new $29.9 million, 10 year mortgage loan with a fixed interest rate of 5.14% to replace the prior mortgage on the property that had a balance of $24.2 million. After the repayment of the prior mortgage, the partnership distributed to proceeds of $2.1 million. Our interest in the unconsolidated partnership is 50%.

In June 2011, the unconsolidated partnership that owns The Court at Oxford Valley in Langhorne, Pennsylvania entered into a new $60.0 million, 10 year mortgage loan with a fixed interest rate of 5.56% to replace the prior mortgage on the property that had a balance of $32.0 million. After the repayment of the prior mortgage, the partnership distributed to us excess proceeds of $12.8 million. Our interest in the unconsolidated partnership is 50%.

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In June 2011, we exercised the first of two one-year extension options on the $45.0 million mortgage loan secured by Christiana Center in Newark, Delaware. In connection with the extension, we now pay principal and interest on the mortgage loan based on a 25 year term.

In June 2011, in connection with the amendment of the 2010 Credit Facility, the lenders released the second mortgage on New River Valley Mall in Christiansburg, Virginia, and that property is no longer one of the collateral properties securing the 2010 Credit Facility.

In July 2011, we entered into a $27.7 million, five year mortgage loan with two one-year extension options secured by a portion of 801 Market Street in Philadelphia, Pennsylvania. The mortgage loan has a variable interest rate of LIBOR plus 2.10%.

In July 2011, we exercised the first of two one-year extension options on the $54.0 million interest only mortgage loan secured by Paxton Towne Centre in Harrisburg, Pennsylvania.

Mortgage Loans

Twenty-six mortgage loans, which are secured by 24 of our consolidated properties, are due in installments over various terms extending to the year 2020. Seventeen of the mortgage loans bear interest at a fixed rate, six of the mortgage loans bear interest at variable rates that have been swapped to fixed rates, two mortgage loans bear interest at a variable rate, and the interest rate on one mortgage loan has been partially swapped to a fixed rate and partially bears interest at a variable rate.

The fixed mortgage loan balances, including mortgage loans that have variable interest rates based on LIBOR, the interest payments on which have been swapped to fixed interest rates, have interest rates that range from 4.95% to 7.61% and had a weighted average interest rate of 5.81% at June 30, 2011. The variable rate mortgage loans had a weighted average interest rate of 2.57% (excluding the spread on the related debt) at June 30, 2011. The weighted average interest rate of all consolidated mortgage loans was 5.72% at June 30, 2011. Mortgage loans for our unconsolidated properties are accounted for in Investments in partnerships, at equity and Distributions in excess of partnership investments on the consolidated balance sheets and are not included in the table below.

The following table outlines the timing of principal payments related to our mortgage loans as of June 30, 2011.

		Payments by Period			
(in thousands of dollars)	**Total**	**2011**	**2012-2013**	**2014-2015**	**Thereafter**
Principal payments	$ 72,256	$ 10,794	$ 33,459	$ 23,516	$ 4,487
Balloon payments[(1)]	1,660,107	58,918	834,668	369,879	396,642
Total	$ 1,732,363	$ 69,712	$ 868,127	$ 393,395	$ 401,129

(1) Due dates for certain of the balloon payments set forth in this table may be extended pursuant to the terms of the respective loan agreements. Of the balloon payments coming due in 2011, $54.0 million was extended in July 2011 under extension options in the loan agreements.

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Contractual Obligations

The following table presents our aggregate contractual obligations as of June 30, 2011 for the periods presented.

(in thousands of dollars)	Total	Remainder of 2011	2012-2013	2014-2015	Thereafter
Mortgage loans [1]	$ 1,732,363	$ 69,712	$ 868,127	$ 393,395	$ 401,129
Exchangeable Notes [2]	136,900		136,900		
2010 Term Loan [3]	240,000			240,000	
Revolving Facility [3]	70,000			70,000	
Interest on indebtedness [4]	370,643	61,397	200,487	85,040	23,719
Operating leases	6,628	1,154	4,021	1,450	3
Ground leases	50,492	470	1,463	1,368	47,191
Development and redevelopment commitments [5]	10,898	10,458	440		
Total	$ 2,617,924	$ 143,191	$ 1,211,438	$ 791,253	$ 472,042

(1) We have eight mortgages secured by seven properties that are scheduled to mature by their terms in the remainder of 2011 or in 2012 with an aggregate balance of $471.5 million. We expect to refinance these mortgages with new mortgages secured by the underlying properties, or to extend the maturity according to the terms of the specific mortgage loan, or, to the extent that we are unable to obtain mortgages for these properties on terms that are satisfactory to us, or at all, we expect to utilize the Revolving Facility to repay the amounts outstanding under such mortgages.

(2) The Exchangeable Notes are due in the second quarter of 2012. We currently anticipate that the sources of funds for repayment might include excess proceeds of mortgage loan refinancings, property sales, the Revolving Facility, or other sources.

(3) The 2010 Credit Facility, which is comprised of the 2010 Term Loan and the Revolving Facility, has a variable interest rate that ranges between 2.75% and 4.00% plus LIBOR depending on our total leverage ratio.

(4) Includes payments expected to be made in connection with interest rate swaps, caps and forward starting interest rate swap agreements.

(5) The timing of the payments of these amounts is uncertain. We expect that substantially all of such payments will be made prior to December 31, 2011, but cannot provide any assurances that changed circumstances at these projects will not delay the settlement of these obligations.

CASH FLOWS

Net cash provided by operating activities totaled $51.8 million for the six months ended June 30, 2011 compared to $62.1 million for the six months ended June 30, 2010. This decrease in cash from operating activities was primarily due to decreased net operating income as the result of a $1.5 million decrease in lease termination revenue, increased common area maintenance expenses and real estate taxes, and the disposition of five power centers in September 2010.

Cash flows provided by investing activities were $0.1 million for the six months ended June 30, 2011 compared to cash flows used in investing activities of $15.1 million for the six months ended June 30, 2010. Investing activities for the six months ended June 30, 2011 reflect investment in construction in progress of $5.0 million and real estate improvements of $17.3 million, primarily relating to our ongoing maintenance of our properties and $7.3 million of proceeds from sales of real estate. Investing activities also reflect $14.9 million in proceeds related to mortgage loans at two of our unconsolidated properties. Investing activities for the six months ended June 30, 2010 reflect

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investment in construction in progress of $12.9 million and real estate improvements of $7.2 million, which primarily relate to our development and redevelopment activities, offset by a $10.0 million decrease in notes receivable from tenants.

Cash flows used in financing activities were $70.0 million for the six months ended June 30, 2011 compared to cash flows used in financing activities of $92.0 million for the six months ended June 30, 2010. Cash flows used in financing activities for the six months ended June 30, 2011 included dividends and distributions of $17.4 million and principal installments on mortgage loans of $10.3 million. Cash flows used in financing activities also reflect a $30.0 million paydown of the Revolving Facility and a $7.2 million paydown of the 2010 Term Loan. Cash flows used in financing activities for the six months ended June 30, 2010 reflected the refinancing of our 2003 Credit Facility and 2008 Term Loan. We replaced the $486.0 million outstanding on the 2003 Credit Facility and the $170.0 million 2008 Term Loan with $590.0 million in proceeds from the 2010 Credit Facility. We paid $15.7 million in deferred financing costs in the six months ended June 30, 2010, primarily relating to this refinancing. We also received $32.5 million in proceeds from a $30.0 million mortgage loan on New River Valley Mall and an additional $2.5 million draw on the mortgage loan at Lycoming Mall in the six months ended June 30, 2010.

COMMITMENTS

In connection with our redevelopment project and capital improvements at certain other properties, we have made contractual and other commitments in the form of tenant allowances, lease termination fees and contracts with general contractors and other professional service providers. As of June 30, 2011, the unaccrued remainder to be paid against these contractual and other commitments was $10.9 million, which is expected to be financed through our Revolving Facility, operating cash flows or through various other capital sources. The projects on which these commitments have been made have total expected remaining costs of $84.6 million. We expect to finance these amounts through borrowings under the 2010 Credit Facility or through various other capital sources. See Liquidity and Capital Resources Capital Resources.

ENVIRONMENTAL

We are aware of certain environmental matters at some of our properties, including ground water contamination and the presence of asbestos containing materials. We have, in the past, performed remediation of such environmental matters, and we are not aware of any significant remaining potential liability relating to these environmental matters. We may be required in the future to perform testing relating to these matters. We have insurance coverage for certain environmental claims up to $10.0 million per occurrence and up to $20.0 million in the aggregate.

COMPETITION AND TENANT CREDIT RISK

Competition in the retail real estate industry is intense. We compete with other public and private retail real estate companies, including companies that own or manage malls, strip centers, power centers, lifestyle centers, factory outlet centers, theme/festival centers and community centers, as well as other commercial real estate developers and real estate owners, particularly those with properties near our properties, on the basis of several factors, including location and rent charged. We compete with these companies to attract customers to our properties, as well as to attract anchor and in-line store tenants. We also compete to acquire land for new site development, during more favorable economic conditions. Our malls and our strip and power centers face competition from similar retail centers, including more recently developed or renovated centers that are near our retail properties. We also face competition from a variety of different retail formats, including internet retailers, discount or value retailers, home shopping networks, mail order operators, catalogs, and telemarketers. This competition could have a material adverse effect on our ability to lease space and on the amount of rent and expense reimbursements that we receive. Our tenants face competition from companies at the same and other properties and from other retail formats as well.

The development of competing retail properties and the related increased competition for tenants might require us to make capital improvements to properties that we would have deferred or would not have otherwise planned to make and might also affect the occupancy and net operating income of such properties. Any such capital improvements, undertaken individually or collectively, would be subject to the terms and conditions of the 2010 Credit Facility and involve costs and expenses that could adversely affect our results of operations.

We compete with many other entities engaged in real estate investment activities for acquisitions of malls, other retail properties and other prime development sites, including institutional pension funds, other REITs and other

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owner-operators of retail properties. Our efforts to compete are also subject to the terms and conditions of our 2010 Credit Facility. Given current economic, capital market and retail industry conditions, however, there has been substantially less competition with respect to acquisition activity in recent quarters. When we seek to make acquisitions, these competitors might drive up the price we must pay for properties, parcels, other assets or other companies or might themselves succeed in acquiring those properties, parcels, assets or companies. In addition, our potential acquisition targets might find our competitors to be more attractive suitors if they have greater resources, are willing to pay more, or have a more compatible operating philosophy. In particular, larger REITs might enjoy significant competitive advantages that result from, among other things, a lower cost of capital, a better ability to raise capital, a better ability to finance an acquisition, and enhanced operating efficiencies. We might not succeed in acquiring retail properties or development sites that we seek, or, if we pay a higher price for a property and/or generate lower cash flow from an acquired property than we expect, our investment returns will be reduced, which will adversely affect the value of our securities.

We receive a substantial portion of our operating income as rent under long-term leases with tenants. At any time, any tenant having space in one or more of our properties could experience a downturn in its business that might weaken its financial condition. These tenants might defer or fail to make rental payments when due, delay or defer lease commencement, voluntarily vacate the premises or declare bankruptcy, which could result in the termination of the tenant s lease, and could result in material losses to us and harm to our results of operations. Also, it might take time to terminate leases of underperforming or nonperforming tenants and we might incur costs to remove such tenants. Some of our tenants occupy stores at multiple locations in our portfolio, and so the effect of any bankruptcy of those tenants might be more significant to us than the bankruptcy of other tenants. In addition, under many of our leases, our tenants pay rent based on a percentage of their sales. Accordingly, declines in these tenants sales directly affect our results of operations. Also, if tenants are unable to comply with the terms of their leases, we might modify lease terms in ways that are less favorable to us.

In February 2011, Borders Group, Inc. (Borders) filed for bankruptcy protection. At that time, we had 11 stores operated by Borders in our portfolio, three of which closed prior to June 30, 2011, including one store that had a lease expiration in March 2011. In July 2011, Borders determined to liquidate operations, and as a result of this action, the eight remaining stores operated by Borders in our portfolio will close during 2011. In connection with the planned liquidation, in the three months ended June 30, 2011, we recorded write-offs of $0.6 million of straight line rent, net of reserves, and $1.0 million of tenant allowances. We expect that the liquidation of Borders and subsequent closures of the remaining stores in our portfolio will result in the loss of approximately $2.0 million in annual rental revenue from those stores.

SEASONALITY

There is seasonality in the retail real estate industry. Retail property leases often provide for the payment of a portion of rent based on a percentage of a tenant s sales revenue over certain levels. Income from such rent is recorded only after the minimum sales levels have been met. The sales levels are often met in the fourth quarter, during the December holiday season. Also, many new and temporary leases are entered into later in the year in anticipation of the holiday season and a higher number of tenants vacate their space early in the year. As a result, our occupancy and cash flows are generally higher in the fourth quarter and lower in the first quarter. Our concentration in the retail sector increases our exposure to seasonality and is expected to continue to result in a greater percentage of our cash flows being received in the fourth quarter.

INFLATION

Inflation can have many effects on financial performance. Retail property leases often provide for the payment of rent based on a percentage of sales, which may increase with inflation. Leases may also provide for tenants to bear all or a portion of operating expenses, which may reduce the impact of such increases on us. However, rent increases might not keep up with inflation, or if we recover a smaller proportion of property operating expenses, we might bear more costs if such expenses increase because of inflation.

FORWARD LOOKING STATEMENTS

This Quarterly Report on Form 10-Q for the quarter ended June 30, 2011, together with other statements and information publicly disseminated by us, contain certain forward-looking statements within the meaning of the

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U.S. Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. Forward-looking statements relate to expectations, beliefs, projections, future plans, strategies, anticipated events, trends and other matters that are not historical facts. These forward-looking statements reflect our current views about future events, achievements or results and are subject to risks, uncertainties and changes in circumstances that might cause future events, achievements or results to differ materially from those expressed or implied by the forward-looking statements. In particular, our business might be materially and adversely affected by uncertainties affecting real estate businesses generally as well as the following, among other factors:

our substantial debt and our high leverage ratio;

constraining leverage, interest and tangible net worth covenants under our 2010 Credit Facility;

our ability to refinance our existing indebtedness when it matures, on favorable terms, or at all;

our ability to raise capital, including through the issuance of equity or equity-related securities if market conditions are favorable, through joint ventures or other partnerships, through sales of properties, or through other actions;

our short- and long-term liquidity position;

the effects on us of dislocations and liquidity disruptions in the capital and credit markets;

current economic conditions and their effect on employment, consumer confidence and spending; tenant business performance, prospects, solvency and leasing decisions; and the value and potential impairment of our properties;

general economic, financial and political conditions, including credit market conditions, changes in interest rates or unemployment;

increases in operating costs that cannot be passed on to tenants;

our ability to maintain and increase property occupancy, sales and rental rates, including at our redeveloped properties;

risks relating to development and redevelopment activities;

changes in the retail industry, including consolidation and store closings;

the effects of online shopping and other uses of technology on our retail tenants;

concentration of our properties in the Mid-Atlantic region;

changes in local market conditions, such as the supply of or demand for retail space, or other competitive factors;

potential dilution from any capital raising transactions;

possible environmental liabilities;

our ability to obtain insurance at a reasonable cost; and

existence of complex regulations, including those relating to our status as a REIT, and the adverse consequences if we were to fail to qualify as a REIT.

Additional factors that might cause future events, achievements or results to differ materially from those expressed or implied by our forward-looking statements include those discussed in our Annual Report on Form 10-K for the year ended December 31, 2010 in the section entitled Item 1A. Risk Factors. We do not intend to update or revise any forward-looking statements to reflect new information, future events or otherwise.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

The analysis below presents the sensitivity of the market value of our financial instruments to selected changes in market interest rates. As of June 30, 2011, our consolidated debt portfolio consisted primarily of $240.0 million borrowed under our 2010 Term Loan, which bore interest at a weighted average interest rate of 5.78%, $70.0 million borrowed under our Revolving Facility, which bore interest at a rate of 5.55%, $136.9 million of Exchangeable Notes, which bear interest at 4.00%, excluding debt discount of $1.8 million, and $1,733.4 million in fixed and variable rate mortgage loans, including $1.0 million of mortgage debt premium.

Twenty-six mortgage loans, which are secured by 24 of our consolidated properties, are due in installments over various terms extending to the year 2020. Seventeen of the mortgage loans bear interest at a fixed rate, six of the mortgage loans bear interest at variable rates that have been swapped to fixed rates, two mortgage loans bear interest at a variable rate, and one mortgage loan has been partially swapped to a fixed rate and partially bears interest at a variable rate.

The fixed mortgage loan balances, including mortgage loans that have variable interest rates based on LIBOR, the interest payments on which have been swapped to fixed interest rates, have interest rates that range from 4.95% to 7.61% and had a weighted average interest rate of 5.81% at June 30, 2011. The variable rate mortgage loans had a weighted average interest rate of 2.57% (excluding the spread on the related debt) at June 30, 2011. The weighted average interest rate of all consolidated mortgage loans was 5.72% at June 30, 2011. Mortgage loans for our unconsolidated properties are accounted for in Investments in partnerships, at equity and Distributions in excess of partnership investments on the consolidated balance sheets and are not included in the table below.

Our interest rate risk is monitored using a variety of techniques. The table below presents the principal amounts of the expected annual maturities and the weighted average interest rates for the principal payments in the specified periods:

	Fixed Rate Debt		Variable Rate Debt	
(in thousands of dollars)		**Weighted**		**Weighted**
Year ending December 31,	**Principal Payments**	**Average Interest Rate**	**Principal Payments**	**Average Interest Rate**
2011	$ 64,429	5.83%	$ 5,283	1.59%[1]
2012	$ 515,731[2]	5.45%	$ 44,635	2.55%
2013	$ 441,612	5.48%	$ 3,0500[4]	4.75%[1]
2014	$ 411,436[3]	6.04%	$ 10,000[3]	4.19%
2015	$ 281,959	5.81%		
2016 and thereafter	$ 401,128	5.65%		

(1) Based on the weighted average interest rate in effect as of June 30, 2011.

(2) Includes Exchangeable Notes of $136.9 million with a fixed interest rate of 4.00%.

(3) Includes $310.0 million of the 2010 Credit Facility. We have entered into interest rate swap agreements to effectively fix $300.0 million of the underlying LIBOR based interest payments associated with the 2010 Credit Facility until March 10, 2013 at a current weighted average rate of 1.78% (excluding the spread on the related debt). Of that notional amount, $200.0 million of this $300.0 million is also covered by a forward starting swap that becomes effective on April 2, 2012 until March 10, 2013 at a rate of 2.96% (which will affect the weighted average rate during that period), excluding the spread on the related debt.

Changes in market interest rates have different effects on the fixed and variable portions of our debt portfolio. A change in market interest rates applicable to the fixed portion of the debt portfolio affects the fair value, but it has no effect on interest incurred or cash flows. A change in market interest rates applicable to the variable portion of the debt portfolio affects the interest incurred and cash flows, but does not affect the fair value. The following sensitivity analysis related to the fixed debt portfolio, which includes the effects of our interest rate swap agreements, assumes an immediate 100 basis point change in interest rates from their actual June 30, 2011 levels, with all other variables held constant.

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A 100 basis point increase in market interest rates would have resulted in a decrease in our net financial instrument position of $57.5 million at June 30, 2011. A 100 basis point decrease in market interest rates would have resulted in an increase in our net financial instrument position of $59.1 million at June 30, 2011. Based on the variable rate debt included in our debt portfolio as of June 30, 2011, a 100 basis point increase in interest rates would have resulted in an additional $0.6 million in interest annually. A 100 basis point decrease would have reduced interest incurred by $0.6 million annually.

To manage interest rate risk and limit overall interest cost, we may employ interest rate swaps, options, forwards, caps and floors, or a combination thereof, depending on the underlying exposure. Interest rate differentials that arise under swap contracts are recognized in interest expense over the life of the contracts. If interest rates rise, the resulting cost of funds is expected to be lower than that which would have been available if debt with matching characteristics was issued directly. Conversely, if interest rates fall, the resulting costs would be expected to be higher. We may also employ forwards or purchased options to hedge qualifying anticipated transactions. Gains and losses are deferred and recognized in net income in the same period that the underlying transaction occurs, expires or is otherwise terminated. See note 7 of the notes to our unaudited consolidated financial statements.

As of June 30, 2011, we had an aggregate $687.5 million in notional amount of swap agreements settling on various dates through November 2013. We also had an aggregate of $200.0 million in notional amount of forward starting interest rate swap agreements maturing on various dates through March 2013.

Because the information presented above includes only those exposures that existed as of June 30, 2011, it does not consider changes, exposures or positions which could arise after that date. The information presented herein has limited predictive value. As a result, the ultimate realized gain or loss or expense with respect to interest rate fluctuations will depend on the exposures that exist, our hedging strategies and interest rates.

ITEM 4. CONTROLS AND PROCEDURES.

We are committed to providing accurate and timely disclosure in satisfaction of our SEC reporting obligations. In 2002, we established a Disclosure Committee to formalize our disclosure controls and procedures. Our Chief Executive Officer and Chief Financial Officer have evaluated the effectiveness of our disclosure controls and procedures as of June 30, 2011, and have concluded as follows:

Our disclosure controls and procedures are designed to ensure that the information that we are required to disclose in our reports under the Securities Exchange Act of 1934 (the Exchange Act) is recorded, processed, summarized and reported within the time periods specified in the SEC s rules and forms.

Our disclosure controls and procedures are effective to ensure that information that we are required to disclose in our Exchange Act reports is accumulated and communicated to management, including our principal executive and principal financial officers, as appropriate, to allow timely decisions regarding required disclosure.

There was no change in our internal controls over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, our internal controls over financial reporting.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS.

In the normal course of business, we have become and might in the future become involved in legal actions relating to the ownership and operation of our properties and the properties that we manage for third parties. In management s opinion, the resolution of any such pending legal actions are not expected to have a material adverse effect on our consolidated financial position or results of operations.

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ITEM 1A. RISK FACTORS.

In addition to the other information set forth in this report, you should carefully consider the risks that could materially affect our business, financial condition or results of operations, which are discussed under the caption Risk Factors in Part I, Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2010.

ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.

Issuer Purchases of Equity Securities

The following table shows the total number of shares that we acquired in the three months ended June 30, 2011 and the average price paid per share.

Period		Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as part of Publicly Announced Plans or Programs	Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs
April 1	April 30, 2011		$		$
May 1	May 31, 2011				
June 1	June 30, 2011				
Total			$		$

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ITEM 6. EXHIBITS.

10.1	Form of Annual Incentive Compensation Opportunity Award for Officers other than the Named Executive Officers.
10.2	Form of Annual Incentive Compensation Opportunity Award for the Company s Chief Executive Officer, the three other members of the Company s Office of the Chair and the Chief Financial Officer, filed as Exhibit 10.1 to the Current Report on Form 8-K dated July 26, 2011, is incorporated herein reference.
10.3	First Amendment dated June 29, 2011 to Amended, Restated and Consolidated Credit Agreement dated as of March 11, 2010 by and among PREIT Associates, L.P. and PREIT-RUBIN, Inc., PR Gallery I Limited Partnership and Keystone Philadelphia Properties, L.P., Pennsylvania Real Estate Investment Trust, and the financial institutions party thereto, filed as Exhibit 10.1 to the Current Report on Form 8-K dated June 29, 2011, is incorporated herein reference.
31.1	Certification pursuant to Exchange Act Rules 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification pursuant to Exchange Act Rules 13a-14(a)/15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Pursuant to Rule 405 of Regulation S-T, the following financial information from the Company s Quarterly Report on Form 10-Q for the period ended June 30, 2011 is formatted in XBRL interactive data files: (i) Consolidated Statements of Operations for the three and six months ended June 30, 2011 and 2010; (ii) Consolidated Balance Sheets as of June 30, 2011 and December 31, 2010; (iii) Consolidated Statements of Equity and Comprehensive Income for the three and six months ended June 30, 2011 and 2010; (iv) Consolidated Statements of Cash Flows for the six months ended June 30, 2011 and 2010; and (v) Notes to Unaudited Consolidated Financial Statements.*

* As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.

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SIGNATURE OF REGISTRANT

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

PENNSYLVANIA REAL ESTATE INVESTMENT TRUST

Date: August 1, 2011

By: /s/ Ronald Rubin
Ronald Rubin

Chief Executive Officer

By: /s/ Robert F. McCadden
Robert F. McCadden

Executive Vice President and Chief Financial Officer

By: /s/ Jonathen Bell
Jonathen Bell

Senior Vice President Chief Accounting Officer

(Principal Accounting Officer)

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Exhibit Index

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* filed herewith

** furnished herewith

*** As provided in Rule 406T of Regulation S-T, this information is furnished and not filed for purposes of Sections 11 and 12 of the Securities Act of 1933 and Section 18 of the Securities Exchange Act of 1934.