UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2019

Commission File Number 001-37799

Tactile Systems Technology, Inc.

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**1331 Tyler Street NE, Suite 200** **Minneapolis, Minnesota 55413** (Address and Zip Code of principal executive offices)	**41-1801204** (I.R.S. employer identification number)

(612) 355-5100

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☑ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes ☑ No ☐

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

Large accelerated filer	☑	Accelerated filer	☐	Non-accelerated filer	☐
Smaller reporting company	☐	Emerging growth company	☐		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

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

Title of each class	**Trading Symbol(s)**	**Name of each exchange on which registered**
Common Stock, Par Value $0.001 Per Share	TCMD	The Nasdaq Stock Market

18,825,688 shares of common stock, par value $0.001 per share, were outstanding as of May 2, 2019.

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PART II—OTHER INFORMATION

Forward-Looking Information

All statements, other than statements of historical facts, contained in this Quarterly Report on Form 10-Q, including statements regarding our business, operations and financial performance and condition, as well as our plans, objectives and expectations for our business, operations and financial performance and condition, are forward-looking statements. In some cases, you can identify forward-looking statements by the following words: "anticipate," "believe," "continue," "could," "estimate," "expect," "intend," "may," "might," "target," "ongoing," "plan," "potential," "predict," "project," "should," "will," "would," or the negative of these terms or other comparable terminology, although not all forward-looking statements contain these words. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our results, levels of activity, performance or achievements to be materially different from the information expressed or implied by the forward-looking statements in this Quarterly Report on Form 10-Q. These risks, uncertainties and other factors include, but are not limited to:

- the adequacy of our liquidity to pursue our complete business objectives;
- our ability to obtain reimbursement from third-party payers for our products;
- loss or retirement of key executives;
- adverse economic conditions or intense competition;
- loss of a key supplier;
- entry of new competitors and products;
- adverse federal, state and local government regulation;
- technological obsolescence of our products;
- technical problems with our research and products;
- our ability to expand our business through strategic acquisitions;
- our ability to integrate acquisitions and related businesses;
- price increases for supplies and components;
- the effects of current and future U.S. and foreign trade policy and tariff actions; and
- the inability to carry out research, development and commercialization plans.

You should read the matters described in "Risk Factors" and the other cautionary statements made in our Annual Report on Form 10-K for the year ended December 31, 2018 and in this Quarterly Report on Form 10-Q. We cannot assure you that the forward-looking statements in this report will prove to be accurate and therefore you are encouraged not to place undue reliance on forward-looking statements. Actual results or events could differ materially from the plans, intentions and expectations disclosed in the forward-looking statements we make. You are urged to carefully review and consider the various disclosures made by us in this report and in other filings with the Securities and Exchange Commission (the “SEC”) that advise of the risks and factors that may affect our business. Other than as required by law, we undertake no obligation to update or revise these forward-looking statements, even though our situation may change in the future. Our forward-looking statements do not reflect the potential impact of any future acquisitions, mergers, dispositions, joint ventures or investments that we may make.

PART I—FINANCIAL INFORMATION

Item 1. Financial Statements

Tactile Systems Technology, Inc.
Condensed Consolidated Balance Sheets
(Unaudited)

(In thousands, except share and per share data)		March 31, 2019		December 31, 2018
ASSETS				
Current assets:				
Cash and cash equivalents	$	23,548	$	20,099
Marketable securities		21,384		25,786
Accounts receivable, net		21,661		24,332
Net investment in leases		3,362		—
Inventories		11,321		11,189
Income taxes receivable		2,814		1,793
Prepaid expenses and other current assets		1,680		1,762
Total current assets		85,770		84,961
Non-current assets:				
Property and equipment, net		4,616		4,810
Right of use operating lease assets		3,396		—
Intangible assets, net		5,244		5,339
Medicare accounts receivable, long-term		2,172		1,884
Deferred income taxes		11,077		8,820
Other non-current assets		1,242		1,257
Total non-current assets		27,747		22,110
Total assets	$	113,517	$	107,071
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities:				
Accounts payable	$	5,832	$	5,110
Accrued payroll and related taxes		6,837		7,421
Accrued expenses		2,685		2,780
Future product royalties		3		5
Income taxes		—		51
Right of use operating lease liabilities		1,147		—
Other current liabilities		800		709
Total current liabilities		17,304		16,076
Non-current liabilities:				
Accrued warranty reserve, non-current		1,854		1,725
Income taxes, non-current		42		—
Right of use operating lease liabilities, non-current		2,318		—
Total non-current liabilities		4,214		1,725
Total liabilities		21,518		17,801
Commitments and contingencies (see Note 10)				
Stockholders' equity:				
Preferred stock, $0.001 par value, 50,000,000 shares authorized; none issued and outstanding as of March 31, 2019 and December 31, 2018		—		—
Common stock, $0.001 par value, 300,000,000 shares authorized; 18,818,692 shares issued and outstanding as of March 31, 2019; 18,631,125 shares issued and outstanding as of December 31, 2018		19		19
Additional paid-in capital		80,788		79,554
Retained earnings		11,177		9,705
Accumulated other comprehensive income (loss)		15		(8)
Total stockholders' equity		91,999		89,270
Total liabilities and stockholders' equity	$	113,517	$	107,071

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tactile Systems Technology, Inc.
Condensed Consolidated Statements of Operations
(Unaudited)

(In thousands, except share and per share data)	Three Months Ended March 31, 2019	2018
Revenue		
Sales revenue	$ 30,831	$ 23,647
Rental revenue	6,786	3,201
Total revenue	37,617	26,848
Cost of revenue		
Cost of sales revenue	9,412	6,409
Cost of rental revenue	1,947	900
Total cost of revenue	11,359	7,309
Gross profit		
Gross profit - sales revenue	21,419	17,238
Gross profit - rental revenue	4,839	2,301
Gross profit	26,258	19,539
Operating expenses		
Sales and marketing	17,391	12,557
Research and development	1,281	1,437
Reimbursement, general and administrative	9,388	7,372
Total operating expenses	28,060	21,366
Loss from operations	(1,802)	(1,827)
Other income	161	91
Loss before income taxes	(1,641)	(1,736)
Income tax benefit	(3,113)	(1,686)
Net income (loss)	$ 1,472	$ (50)
Net income per common share		
Basic	$ 0.08	$ 0.00
Diluted	$ 0.08	$ 0.00
Weighted-average common shares used to compute net income per common share		
Basic	18,746,751	17,996,672
Diluted	19,579,847	17,996,672

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tactile Systems Technology, Inc.
Condensed Consolidated Statements of Comprehensive Income
(Unaudited)

(In thousands)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Net income (loss)	$ 1,472	$ (50)
Other comprehensive income (loss):		
Unrealized gain (loss) on marketable securities	30	(7)
Income tax related to items of other comprehensive income (loss)	(7)	1
Total other comprehensive income (loss)	23	(6)
Comprehensive income (loss)	$ 1,495	$ (56)

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements

Tactile Systems Technology, Inc.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)

(In thousands, except share data)	Common Stock Shares	Common Stock Par Value	Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive (Loss) Income	Treasury Stock	Total
Balances, December 31, 2017	17,846,379	$ 18	$ 70,224	$ 3,082	$ (44)	$ (493)	$ 72,787
Stock-based compensation	—	—	1,481	—	—	—	1,481
Exercise of common stock options and vesting of restricted stock units	230,532	—	138	—	—	—	138
Taxes paid for net share settlement of restricted stock units	(40,202)	—	(1,188)	—	—	—	(1,188)
Comprehensive loss for the period	—	—	—	(50)	(6)	—	(56)
Balances, March 31, 2018	18,036,709	$ 18	$ 70,655	$ 3,032	$ (50)	$ (493)	$ 73,162
Balances, December 31, 2018	18,631,125	19	79,554	9,705	(8)	—	89,270
Stock-based compensation	—	—	2,783	—	—	—	2,783
Exercise of common stock options and vesting of restricted stock units	231,814	—	861	—	—	—	861
Taxes paid for net share settlement of restricted stock units	(44,247)	—	(2,410)	—	—	—	(2,410)
Comprehensive income for the period	—	—	—	1,472	23	—	1,495
Balances, March 31, 2019	18,818,692	$ 19	$ 80,788	$ 11,177	$ 15	$ —	$ 91,999

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tactile Systems Technology, Inc.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

(In thousands)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Cash flows from operating activities		
Net income (loss)	$ 1,472	$ (50)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	996	463
Deferred income taxes	(2,264)	—
Stock-based compensation expense	2,783	1,481
Changes in assets and liabilities:		
Accounts receivable	2,671	3,414
Net investment in leases	(3,362)	—
Inventories	(132)	(3,616)
Income taxes	(1,030)	(1,952)
Prepaid expenses and other assets	97	63
Right of use operating lease assets	(3,396)	—
Medicare accounts receivable – long-term	(288)	(253)
Accounts payable	722	885
Accrued payroll and related taxes	(584)	(1,850)
Accrued expenses and other liabilities	125	(756)
Right of use operating lease liabilities	3,465	—
Future product royalties	(2)	(2)
Net cash provided by (used in) operating activities	1,273	(2,173)
Cash flows from investing activities		
Proceeds from sales of securities available-for-sale	—	1,000
Proceeds from maturities of securities available-for-sale	4,500	4,000
Purchases of property and equipment	(731)	(432)
Intangible assets costs	(44)	—
Net cash provided by investing activities	3,725	4,568
Cash flows from financing activities		
Taxes paid for net share settlement of restricted stock units	(2,410)	(1,188)
Proceeds from exercise of common stock options	861	138
Net cash used in financing activities	(1,549)	(1,050)
Net increase in cash and cash equivalents	3,449	1,345
Cash and cash equivalents – beginning of period	20,099	23,968
Cash and cash equivalents – end of period	$ 23,548	$ 25,313
Supplemental cash flow disclosure		
Cash paid for interest	$ —	$ —
Cash paid for taxes	$ 181	$ 284
Capital expenditures incurred but not yet paid	$ 176	$ 96

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

Tactile Systems Technology, Inc.
Notes to the Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Nature of Business and Operations

Tactile Systems Technology, Inc. ("we," "us," and "our") is the sole manufacturer and distributor of the Flexitouch and Entre systems, medical devices that help control symptoms of lymphedema, a chronic and progressive medical condition, the Actitouch system, a medical device used to treat venous leg ulcers and chronic venous insufficiency, and the Airwear wrap, a medical device used for the management of venous insufficiency, venous hypertension, venous ulcerations and lymphedema. We provide our products for use in the home and sell or rent them through vascular, wound and lymphedema clinics throughout the United States. We do business as "Tactile Medical."

We were originally incorporated in Minnesota under the name Tactile Systems Technology, Inc. on January 30, 1995. During 2006, we established a merger corporation and subsequently, on July 21, 2006, merged with and into this merger corporation, resulting in us being reincorporated as a Delaware corporation. The resulting corporation assumed the name Tactile Systems Technology, Inc. In September 2013, we began doing business as "Tactile Medical."

On August 2, 2016, we closed the initial public offering of our common stock, which resulted in the sale of 4,120,000 shares of our common stock at a public offering price of $10.00 per share. We received net proceeds from the initial public offering of approximately $35.4 million, after deducting underwriting discounts and approximately $2.9 million of transaction expenses. In connection with the closing of the initial public offering, all of our outstanding redeemable convertible preferred stock automatically converted to common stock on August 2, 2016. At August 2, 2016, we did not have any redeemable convertible preferred stock issued or outstanding.

Our business is affected by seasonality. In the first quarter of each year, when most patients have started a new insurance year and have not yet met their annual out-of-pocket payment obligations, we experience substantially reduced demand for our products. We typically experience higher revenues in the third and fourth quarters as a result of patients having paid their annual insurance deductibles in full, thereby reducing their out-of-pocket costs for our products, and because patients often spend the remaining balances in their healthcare flexible spending accounts at that time. This seasonality applies only to purchases and rentals of our products by patients covered by commercial insurance and is not relevant to Medicare, Medicaid or the Veterans Administration, as those payers either do not have plans that have declining deductibles over the course of the plan year or do not have plans that include patient deductibles for purchases or rentals of our products.

Note 2. Basis of Presentation

Our accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial reporting and pursuant to the rules and regulations of the SEC. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments (including those which are normal and recurring) considered necessary for a fair presentation of the interim financial information have been included. We have reclassified certain prior year amounts to conform to the current year's presentation.

The results for the three months ended March 31, 2019 are not necessarily indicative of results to be expected for the year ending December 31, 2019, or for any other interim period or for any future year. The condensed consolidated interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2018.

Principles of Consolidation

Our accompanying unaudited condensed consolidated financial statements include the accounts of Tactile Systems Technology, Inc. and its wholly owned subsidiary, Swelling Solutions, Inc. All intercompany balances and transactions have been eliminated in consolidation.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and to disclose contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Comprehensive Income

Comprehensive income reflects the change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources. Our comprehensive income represents net income adjusted for unrealized gains and losses on available-for-sale marketable securities.

JOBS Act Accounting Election

Prior to December 31, 2018, we were an “emerging growth company” as defined by the Jumpstart Our Business Startups Act of 2012 (the “JOBS Act”) and as a result we were eligible to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not emerging growth companies. We elected to take advantage of the extended transition period for adopting new or revised accounting standards that have different effective dates for public and private companies until such time as those standards apply to private companies. However, as of the last business day of our second fiscal quarter of 2018, the market value of our common stock that was held by non-affiliates exceeded $700 million, and as a result, we no longer qualified as an emerging growth company as of December 31, 2018 and are no longer able to take advantage of the extended transition period for adopting new or revised accounting standards. Therefore, beginning December 31, 2018, we were required to adopt new or revised accounting standards when they are applicable to public companies that are not emerging growth companies.

Note 3. Summary of Significant Accounting Policies

Significant Accounting Policies

Excluding the adoption of ASC 842 “Leases”, as described below, there were no material changes in our significant accounting policies during the three months ended March 31, 2019. See Note 3 - “Summary of Significant Accounting Policies” to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2018 for information regarding our significant accounting policies.

Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2016-02, “Leases” (Topic 842) (“ASC 842”), which supersedes the existing guidance for lease accounting, “Leases” (Topic 840) (“ASC 840”). ASC 842 requires lessees to recognize a lease liability and a right of use asset for all leases that extend beyond one year. As a result of our change in filing status, we adopted this standard using the modified retrospective transition approach at the adoption date of January 1, 2019. This approach does not require restatement of previous periods. We completed a qualitative and quantitative assessment of our leases from both a lessee and lessor perspective. As part of our process, we elected to utilize certain practical expedients that were provided for transition relief. Accordingly, we did not reassess expired or existing contracts, lease classifications or related initial direct costs as part of our assessment process for either lessee or lessor leases. Additionally, we elected the practical expedient to treat lease and nonlease components of fixed payments due to the lessor as one, and therefore no separate allocation was required on the initial implementation date of January 1, 2019, and thereafter. The adoption of this standard, from a lessee perspective, resulted in us recording Right of Use ("ROU") operating lease assets and liabilities of approximately $3.1 million on the Condensed Consolidated Balance Sheet as of January 1, 2019, with no impact to retained earnings. In addition, we elected as an accounting policy, not to record leases with an initial term of less than 12 months. From a lessor perspective, the application of ASC 842 to our rental revenue, which was recognized as month-to-month, cancelable leases in accordance with ASC 840 through December 31, 2018, resulted in recognizing rental revenue as a sales-type lease under ASC 842 thereafter. Rental sales agreements that commenced prior to December 31, 2018, will continue to be recognized as month-to-month, cancelable leases until they are completed, as we elected the practical expedient to not reassess the lease classification for leases in existence upon adoption. As such, rental agreements commencing after January 1, 2019 were recorded as sales-type leases with the associated revenue and cost of revenue recognized on the lease commencement date and a corresponding net investment in leases on the Condensed Consolidated Balance Sheet. (See Note 10 – "Commitments and Contingencies" and Note 12 – "Revenue" for additional information and required disclosures.)

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments — Credit Losses," to require the measurement of expected credit losses for financial instruments held at the reporting date based on historical experience, current conditions and reasonable forecasts. The ASU will be effective for us for interim and annual periods beginning January 1, 2020. Therefore, we plan to further evaluate the anticipated impact of the adoption of this ASU on our condensed consolidated financial statements in future periods.

In July 2018, the FASB issued ASU No. 2018-07 "Improvements to Non-employee Share-Based Payment Accounting," which expands the scope of ASC 718 – "Stock Based Compensation" to include share-based payment transactions for acquiring goods and services from non-employees. The ASU was effective for us beginning January 1, 2019, including interim periods within the fiscal year. We have early adopted ASU 2018-07 for the quarter ended March 31, 2019 and it did not have a material impact on our condensed consolidated financial statements.

Note 4. Marketable Securities

Our investments in marketable securities, all of which have original contractual maturities of ten to twenty-four months, are classified as available-for-sale and consist of the following:

	At March 31, 2019			
	Amortized	Unrealized		Fair
(In thousands)	Cost	Gains	Losses	Value
U.S. government and agency obligations	$ 17,391	$ 13	$ 3	$ 17,401
Corporate debt securities and certificates of deposit	3,973	11	1	3,983
Marketable securities	$ 21,364	$ 24	$ 4	$ 21,384

	At December 31, 2018			
	Amortized	Unrealized		Fair
(In thousands)	Cost	Gains	Losses	Value
U.S. government and agency obligations	$ 19,332	$ 5	$ 17	$ 19,320
Corporate debt securities and certificates of deposit	6,464	7	5	6,466
Marketable securities	$ 25,796	$ 12	$ 22	$ 25,786

Net pre-tax unrealized gains for marketable securities at March 31, 2019, were recorded as a component of accumulated other comprehensive income in stockholders' equity. There were no sales of marketable securities during the three months ended March 31, 2019.

Unrealized losses and fair value of marketable securities aggregated by investment category and the length of time the securities were in a continuous loss position were as follows:

	At March 31, 2019					
	Less than 12 months		12 months or more		Total	
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government and agency obligations	$ 7,474	$ 2	$ 999	$ 1	$ 8,473	$ 3
Corporate debt securities and certificates of deposit	1,498	1	—	—	1,498	1
Marketable securities	$ 8,972	$ 3	$ 999	$ 1	$ 9,971	$ 4

	At December 31, 2018					
	Less than 12 months		12 months or more		Total	
(In thousands)	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
U.S. government and agency obligations	$ 11,884	$ 11	$ 2,993	$ 6	$ 14,877	$ 17
Corporate debt securities and certificates of deposit	2,993	3	999	2	3,992	5
Marketable securities	$ 14,877	$ 14	$ 3,992	$ 8	$ 18,869	$ 22

Note 5. Inventories

Inventories consisted of the following:

(In thousands)	At March 31, 2019	At December 31, 2018
Finished goods	$ 4,656	$ 5,318
Component parts and work-in-process	6,665	5,871
Total inventories	$ 11,321	$ 11,189

Note 6. Intangible Assets

Our patents and other intangible assets, all of which are subject to amortization, are summarized as follows:

		At March 31, 2019			At December 31, 2018		
(In thousands)	Weighted-Average Amortization Period	Gross Carrying Amount	Accumulated Amortization	Net Amount	Gross Carrying Amount	Accumulated Amortization	Net Amount
Patents	11 years	$ 4,298	$ 157	$ 4,141	$ 4,253	$ 71	$ 4,182
Defensive intangible assets	5 years	1,126	130	996	1,126	82	1,044
Customer accounts	4 years	125	18	107	125	12	113
Total		$ 5,549	$ 305	$ 5,244	$ 5,504	$ 165	$ 5,339

Amortization expense was $0.1 million for each of the three months ended March 31, 2019 and 2018. Future amortization expenses are expected as follows:

(In thousands)		
2019 (April 1 - December 31)	$	419
2020		558
2021		558
2022		558
2023		491
Thereafter		2,660
Total	$	5,244

Note 7. Accrued Expenses

Accrued expenses consisted of the following:

(In thousands)	At March 31, 2019		At December 31, 2018	
Warranty	$	873	$	841
Legal and consulting		710		319
Travel and business		622		557
Accrued taxes		262		115
Clinical studies		33		60
Acquisition earn-out		—		375
Deferred rent		—		155
Other		185		358
Total	$	2,685	$	2,780

Note 8. Warranty Reserves

The reserve for warranties was as follows:

	Three Months Ended March 31,			
(In thousands)	2019		2018	
Beginning balance	$	2,566	$	1,672
Warranty provision		418		351
Processed warranty claims		(257)		(203)
Ending balance	$	2,727	$	1,820
Accrued warranty reserve, current	$	873	$	648
Accrued warranty reserve, non-current		1,854		1,172
Total accrued warranty reserve	$	2,727	$	1,820

Note 9. Credit Agreement

On August 3, 2018, we entered into a credit agreement with Wells Fargo Bank, National Association. On February 12, 2019, we entered into a first amendment to our credit agreement, which provided for an increase in our annual capital expenditure limitations. On March 25, 2019, we entered into a waiver and second amendment to our credit agreement, which provided that the business plan and budget required to be delivered annually be reduced to cover one year as opposed to the initial three-year coverage requirement. We refer to the credit agreement, as amended, as the "Credit Agreement."

The Credit Agreement provides for a $10.0 million revolving credit facility. The revolving credit facility expires on August 3, 2021. Subject to satisfaction of certain conditions, we may increase the amount of the revolving loans available under the Credit Agreement and/or add one or more term loan facilities in an amount not to exceed an incremental $25.0 million in the aggregate, such that the total aggregate principal amount of loans available under the Credit Agreement (including under the revolving credit facility) does not exceed $35.0 million.

Amounts drawn under the revolving credit facility bear interest, at our option, at a rate equal to (a) the highest of (i) the prime rate, (ii) the federal funds rate plus 0.50% and (iii) LIBOR for an interest period of one month plus 1% (the “Base Rate”) plus an applicable margin or (b) LIBOR plus the applicable margin. The applicable margin is 0.40% to 1.15% on loans bearing interest at the Base Rate and 1.40% to 2.15% on loans bearing interest at LIBOR, in each case depending on our consolidated total leverage ratio. Undrawn portions of the revolving credit facility are subject to an unused line fee at a rate per annum from 0.200% to 0.275%, depending on our consolidated total leverage ratio.

As of March 31, 2019, we did not have any outstanding borrowings under the Credit Agreement.

Note 10. Commitments and Contingencies

Lease Obligations

We lease property and equipment under operating leases, typically with terms greater than 12 months, and determine if an arrangement contains a lease at inception. In general, an arrangement contains a lease if there is an identified asset and we have the right to direct the use of and obtain substantially all of the economic benefit from the use of the identified asset. We record a ROU operating lease liability at the present value of lease payments over the lease term on the commencement date. The related ROU operating lease asset reflects rental escalation clauses as well as renewal options and/or termination options. The exercise of lease renewal and/or termination options are at our discretion and are included in the determination of the lease term and lease payment obligations when it is deemed reasonably certain that the option will be exercised. When available, we use the rate implicit in the lease to discount lease payments to present value; however, certain leases do not provide a readily determinable implicit rate. Therefore, we must estimate our incremental borrowing rate to discount the lease payments based on information available at lease commencement.

We classify our leases as Buildings, Vehicles or Computer/Office Equipment and do not separate lease and nonlease components of contracts for any of the aforementioned classifications. In accordance with applicable guidance, we do not record leases with terms that are less than one year on the Condensed Consolidated Balance Sheet.

None of our lease agreements contain material restrictive covenants or residual value guarantees.

Buildings

We lease certain office and warehouse space at various locations in the United States where we provide services. These leases are typically greater than one year with fixed, escalating rents over the noncancelable terms and therefore, ROU operating lease assets and liabilities are recorded on the Condensed Consolidated Balance Sheet, with rent expense to be recognized on a straight-line basis over the term of the lease. The remaining lease terms vary from approximately 1 to 5 years as of the adoption date of January 1, 2019.

In March 2008, we entered into a noncancelable operating lease agreement for building space for our corporate headquarters that provides for monthly rent, real estate taxes and operating expenses that was subsequently extended to July 31, 2021. This space is included in our ROU operating lease assets and liabilities. We are looking to sub-lease this space for the remainder of our lease obligation due to our new headquarters lease described below.

We entered into a lease in October 2018 for office space for our future corporate headquarters in Minneapolis, Minnesota which will commence upon our move, which is expected to occur in the fourth quarter of 2019. As such, this lease is not included in either the ROU operating lease assets or liabilities. The initial lease term is through February 2030, with an option to renew for two periods of five years each.

Vehicles

We lease vehicles for certain members of our field sales organization under a vehicle fleet program whereby the initial, noncancelable lease is for a term of 367 days, thus more than one year. Subsequent to the initial term, the lease becomes a month-to-month, cancelable lease. As of March 31, 2019, we had approximately 40 vehicles with agreements within the initial, noncancelable lease term that are recorded as ROU operating lease assets and liabilities. In addition to monthly rental fees specific to the vehicle, there are fixed monthly nonlease components that have been included in the ROU operating lease assets and liabilities. The nonlease components are not significant.

Computer and Office Equipment

We also have operating lease agreements for certain computer and office equipment. The remaining lease terms at the adoption date of January 1, 2019 range from seven months to approximately four and a half years with fixed monthly payments that are included in the ROU operating lease assets and liabilities. The leases provide an option to purchase the related equipment at fair market value at the end of the lease. The lease will automatically renew as a month-to-month rental at the end of the lease if the equipment is not purchased or returned.

Lease Position, Undiscounted Cash Flow and Supplemental Information

The table below presents the lease-related assets and liabilities recorded on our Condensed Consolidated Balance Sheet:

(In thousands)		At March 31, 2019
Right of use operating lease assets	$	3,396
Right of use operating lease liabilities:		
Current	$	1,147
Non-current		2,318
Total	$	3,465
Operating leases:		
Weighted average remaining lease term		3.5 years
Weighted average discount rate (1)		5.05%

(1) Discount rates were established as of January 1, 2019, the adoption date

The table below reconciles the undiscounted cash flows under the operating leases recorded on the Condensed Consolidated Balance Sheet for each of the next five years and total of the remaining years:

(In thousands)		
2019 (April 1 - December 31)	$	1,000
2020		1,082
2021		741
2022		456
2023		383
Thereafter		32
Total minimum lease payments		3,694
Less: amount of lease payments representing interest		(229)
Present value of future minimum lease payments		3,465
Less: current obligations under leases		(1,147)
Long-term lease obligations	$	2,318

As of March 31, 2019, we have additional lease commitments of $19.9 million related to our future headquarters that we anticipate will commence in the fourth quarter of 2019. As the lessee we are involved in providing guidance to the lessor for related improvements, however these improvements are managed and owned by the lessor.

Operating lease costs accounted for under ASC 842, for the three months ended March 31, 2019, were $0.3 million. Cash paid for the three months ended March 31, 2019 for operating lease liabilities included in the measurement of the lease liability was $0.3 million.

Rent expense accounted for under ASC 840, for the three months ended March 31, 2018 was $0.3 million.

Major Vendors

We had purchases from three major vendors that accounted for 40% of our total purchases for the three months ended March 31, 2019 and from two major vendors that accounted for 33% of our total purchases for the three months ended March 31, 2018.

Purchase Commitments

We issued purchase orders prior to March 31, 2019, totaling $19.5 million for goods that we expect to receive between April and December of 2019.

Retirement Plan

We maintain a 401(k) retirement plan for our employees in which eligible employees can contribute a percentage of their pre-tax compensation. Discretionary contributions to the 401(k) plan totaled $0.1 million for each of the three months ended March 31, 2019 and 2018.

Note 11. Stockholders' Equity

Stock-Based Compensation

Our 2016 Equity Incentive Plan (the “2016 Plan”) authorizes us to grant stock options, stock appreciation rights, restricted stock, stock units and other stock-based awards to employees, non-employee directors and certain consultants and advisors. There were up to 4,800,000 shares of our common stock initially reserved for issuance pursuant to the 2016 Plan. The 2016 Plan provides that the number of shares reserved and available for issuance under the 2016 Plan will automatically increase annually on January 1 of each calendar year, commencing in 2017 and ending on and including January 1, 2026, by an amount equal to the lesser of: (a) 5% of the number of common shares of stock outstanding as of December 31 of the immediately preceding calendar year, or (b) 2,500,000 shares; provided, however, that our Board of Directors may determine that any annual increase be a lesser number. In addition, all awards granted under our 2007 Omnibus Stock Plan and our 2003 Stock Option Plan that were outstanding when the 2016 Plan became effective and that are forfeited, expire, are cancelled, are settled for cash or otherwise not issued, will become available for issuance under the 2016 Plan. Pursuant to the automatic increase feature of the 2016 Plan, 892,318 and 841,686 shares were added as available for issuance thereunder on January 1, 2018 and 2017, respectively. Our Board of Directors exercised its prerogative to forego the automatic increase on January 1, 2019. As of March 31, 2019, 5,092,296 shares were available for future grant pursuant to the 2016 Plan.

Upon adoption and approval of the 2016 Plan, all of our previous equity incentive compensation plans were terminated. However, existing awards under those plans continue to vest in accordance with the original vesting schedules and will expire at the end of their original terms.

We recorded stock-based compensation expense of $2.8 million and $1.5 million for the three months ended March 31, 2019 and 2018, respectively. This expense was allocated as follows:

(In thousands)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Cost of revenue	$ 98	$ 40
Sales and marketing expenses	1,166	652
Research and development expenses	80	69
Reimbursement, general and administrative expenses	1,439	720
Total stock-based compensation expense	$ 2,783	$ 1,481

The stock-based compensation expense included modifications of share-based awards totaling $0.3 million for the three months ended March 31, 2019. This amount included the acceleration of vesting pursuant to the terms of an employee's award agreement of $0.2 million and a final charge of $0.1 million pertaining to the January 1, 2019 revaluation of the unvested portion of outstanding awards held by a former executive upon our adoption of ASU No. 2018-07 "Improvements to Non-employee Share Based Payment Accounting".

Stock Options

Stock options issued to participants other than non-employees vest over three or four years and typically have a contractual term of seven or ten years. Annually, stock options are granted to our non-employee directors on the date of the annual meeting of stockholders and vest in full on the earlier of one year after the date of grant or on the date of the next year's annual meeting of stockholders. These options have a contractual term of seven years.

Stock-based compensation expense included in our Condensed Consolidated Statements of Operations for stock options was $0.7 million and $0.5 million for the three months ended March 31, 2019 and 2018, respectively.

At March 31, 2019, there was approximately $7.2 million of total unrecognized pre-tax stock option expense under our equity compensation plans, which is expected to be recognized on a straight-line basis over a weighted-average period of 2.9 years.

Stock option activity for the three months ended March 31, 2019 is summarized as follows:

(In thousands except options and per share data)	Options Outstanding	Weighted-Average Exercise Price Per Share [(1)]	Weighted-Average Remaining Contractual Life	Aggregate Intrinsic Value [(2)]
Balance at December 31, 2018	1,076,535	$ 17.94	6.5 years	$ 31,172
Granted	73,948	$ 72.64		
Exercised	(101,016)	$ 8.53		$ 5,731
Forfeited	(10,416)	$ 28.44		
Balance at March 31, 2019	1,039,051	$ 22.64	6.4 years	$ 33,527
Options exercisable at March 31, 2019	586,039	$ 8.57	5.1 years	$ 25,887

(1) The exercise price of each option granted during the period shown was equal to the market price of the underlying stock on the date of grant.

(2) The aggregate intrinsic value of options exercised represents the difference between the exercise price of the option and the closing stock price of our common stock on the date of exercise. The aggregate intrinsic value of options outstanding represents the difference between the exercise price of the option and the closing stock price of our common stock on the last trading day of the period.

Options exercisable of 906,063 as of March 31, 2018 had a weighted-average exercise price of $2.75 per share.

Time-Based Restricted Stock Units

We have granted time-based restricted stock units to certain participants under the 2016 Plan that are stock-settled with common shares. Time-based restricted stock units granted under the 2016 Plan vest over one to three years. Stock-based compensation expense included in our Condensed Consolidated Statements of Operations for time-based restricted stock units was $0.8 million for each of the three-month periods ended March 31, 2019 and 2018. As of March 31, 2019, there was approximately $7.0 million of total unrecognized pre-tax compensation expense related to outstanding time-based restricted stock units that is expected to be recognized over a weighted-average period of 2.2 years.

Our time-based restricted stock unit activity for the three months ended March 31, 2019 was as follows:

(In thousands except unit and per unit data)	Units Outstanding		Weighted-Average Grant Date Fair Value Per Unit		Aggregate Intrinsic Value [(1)]
Balance at December 31, 2018	309,632	$	23.69	$	14,104
Granted	43,258	$	72.38		
Vested	(131,363)	$	15.76		
Cancelled	(244)	$	17.35		
Balance at March 31, 2019	221,283	$	37.92	$	11,666
Deferred and unissued at March 31, 2019[(2)]	4,432	$	35.43	$	234

(1) The aggregate intrinsic value of restricted stock units outstanding was based on our closing stock price on the last trading day of the period.

(2) For the three months ended March 31, 2019, there were 567 restricted stock units granted to non-employee directors in lieu of their quarterly cash retainer payments. These restricted stock units were fully vested upon grant and represent the right to receive one share of common stock, per unit, upon the earlier of the directors' termination of service as a director of ours or the occurrence of a change of control of us. These restricted stock units are included in the "Granted" line in the table above and are also included in the "Vested" line in the table above due to their being fully vested upon grant. As of March 31, 2019, there were 4,432 outstanding restricted stock units that have been previously granted to non-employee directors in lieu of their quarterly director retainer payments. These restricted stock units are not included in the "Balance at March 31, 2019" line in the table above because they are fully vested.

Performance-Based Restricted Stock Units

We have granted performance-based restricted stock units ("PSUs") to certain participants under the 2016 Plan. These PSUs have both performance-based and time-based vesting features. The PSUs granted in 2018 will be earned if and to the extent performance goals based on revenue and adjusted EBITDA are achieved in 2019. The PSUs granted in 2019 will be earned if and to the extent performance goals based on revenue and adjusted EBITDA are achieved in 2020. The number of PSUs earned will depend on the level at which the performance targets are achieved, and can range from 50% of target if threshold performance is achieved and up to 150% of target if maximum performance is achieved. One-third of the earned PSUs will vest on the date the Compensation and Organization Committee certifies the number of PSUs earned, and the remaining two thirds of the earned PSUs will vest on the first anniversary of that certification date. All earned and vested PSUs will be settled in shares of common stock. Stock-based compensation expense included in our Condensed Consolidated Statements of Operations for PSUs was $0.7 million and $0.1 million for the three months ended March 31, 2019 and 2018, respectively. The stock-based compensation expense for the three months ended March 31, 2019 reflects a $0.4 million charge due to a change in the estimated payout to 150% of target for those PSUs granted in 2018. As of March 31, 2019, there was approximately $3.8 million of total unrecognized pre-tax compensation expense related to outstanding PSUs that is expected to be recognized over a weighted average period of 2.4 years.

Our performance-based restricted stock unit activity reflected at target for the three-months ended March 31, 2019 was as follows:

(In thousands except unit and per unit data)	Performance-Based Units Outstanding		Weighted-Average Grant Date Fair Value Per Unit		Aggregate Intrinsic Value (1)
Balance at December 31, 2018	65,427	$	33.62	$	2,980
Granted	25,724	$	72.64		
Vested	—	$	—		
Cancelled	—	$	—		
Balance at March 31, 2019	91,151	$	44.63	$	4,805

(1) The aggregate intrinsic value of performance-based restricted stock units outstanding was based on our closing stock price on the last trading day of the period.

Employee Stock Purchase Plan

Our employee stock purchase plan ("ESPP"), which was approved by our Board of Directors on April 27, 2016 and by our stockholders on June 20, 2016, allows participating employees to purchase shares of our common stock at a discount through payroll deductions. The plan is available to all our employees and employees of participating subsidiaries. Participating employees may purchase common stock, on a voluntary after-tax basis, at a price equal to 85% of the lower of the closing market price per share of our common stock on the first or last trading day of each stock purchase period. The plan provides for six-month purchase periods, beginning on May 16 and November 16 of each calendar year.

A total of 1.6 million shares of common stock was initially reserved for issuance under the ESPP, and this share reserve will automatically be supplemented each January 1, commencing in 2017 and ending on and including January 1, 2026, by an amount equal to the least of (1) 1% of the shares of our common stock outstanding on the immediately preceding December 31, (2) 500,000 shares or (3) such lesser amount as our Board of Directors may determine. Pursuant to the automatic increase feature of the plan, 178,463 and 168,337 shares were added to the ESPP on January 1, 2018 and 2017, respectively. Our Board of Directors exercised its prerogative to forego the automatic increase on January 1, 2019. As of March 31, 2019, 1,542,576 shares were available for future issuance under the ESPP. We recognized stock-based compensation expense associated with the ESPP of $0.3 million for each of the three-month periods ended March 31, 2019 and 2018.

Note 12. Revenue

We derive our revenues from the sale and rental of our Flexitouch, Entre and Actitouch systems to our customers in the United States. While our primary source of revenue is from the sale of our products, a portion of our revenues are derived from patients who obtain our products under rental arrangements. (See description below for additional information on rental revenue as it relates to ASC 842 "Leases".) These arrangements are primarily for rentals of the Flexitouch system and are mostly related to private insurers, and the Veterans Administration.

The following table presents our revenue, inclusive of sales and rental revenue, disaggregated by product:

(In thousands)	Three Months Ended March 31, 2019	2018
Revenues		
Flexitouch system	$ 34,109	$ 24,530
Entre/Actitouch systems	3,508	2,318
Total	$ 37,617	$ 26,848
Percentage of total revenues		
Flexitouch system	91 %	91 %
Entre/Actitouch systems	9 %	9 %
Total	100 %	100 %

Our revenues from third-party payers, inclusive of sales and rental revenue, for the three months ended March 31, 2019 and 2018 are summarized in the following table:

(In thousands)	Three Months Ended March 31, 2019	2018
Private insurers and other payers	$ 25,929	$ 18,115
Veterans Administration	7,670	6,179
Medicare	4,018	2,554
Total	$ 37,617	$ 26,848

Our rental revenue is derived from rent to purchase arrangements that typically range from three to ten months. Under ASC 840, our rental revenue was recognized as month-to-month, cancelable leases, however, because title transfers to the patient, with whom we have the contract, upon the termination of the lease term and because collectability is probable, under ASC 842, these are recognized as sales-type leases. Each rental agreement contains two components, the controller and related garments, both of which are interdependent and recognized as one lease component.

In accordance with applicable guidance, we will continue to recognize rental agreements commencing prior to December 31, 2018 on a month-to-month basis as an operating lease until they are completed, which we anticipate to be in the fourth quarter of this fiscal year. Those initiated subsequent to January 1, 2019 are recorded as sales-type leases in accordance with ASC 842, whereby rental revenue and cost of rental revenue are recognized upon the lease commencement date. Total rental revenue in the three months ended March 31, 2019 includes both operating and sales-type lease revenue. Operating lease revenue for the three months ended March 31, 2019 was $2.8 million. Rental revenue for the three months ended March 31, 2018 related to operating leases under ASC 840 and includes garment revenue of approximately $0.2 million previously included as a purchase.

The revenue and associated cost of revenue of sales-type leases are recognized on the lease commencement date and a net investment in leases is recorded on the Condensed Consolidated Balance Sheet. We bill the patients' insurance payers monthly over the duration of the rental term. We record the net investment in leases and recognize revenue upon commencement of the lease in the amount of the expected consideration to be received through the monthly payments. Similar to our sales revenue, the transaction price is impacted by multiple factors, including the terms and conditions contracted by various third party payers. As the rental contract resides with the patients, we have elected the portfolio approach, at the payer level, to determine the expected consideration, which considers the impact of early terminations. While the contract is with the patient, in certain circumstances, the third party payer elects an initial rental period with an option to extend. We assess the likelihood of extending the lease at the onset of the lease to determine if the option is reasonably certain to be exercised. As the lease is short-term in nature, we anticipate collection of substantially all of the net investment within the first year of the lease agreement. Completion of these payments represents the fair market value of the equipment, and as such, interest income is not applicable.

Sales-type lease revenue and the associated cost of revenue for the three months ended March 31, 2019 was:

	Three Months Ended March 31,
(In thousands)	2019
Sales-type lease revenue	$ 3,965
Cost of sales-type lease revenue	1,543
Gross profit	$ 2,422

Note 13. Income Taxes

We record our interim provision for income taxes by applying our estimated annual effective tax rate to our year-to-date pre-tax income and adjusting for discrete tax items recorded in the period. Deferred income taxes result from temporary differences between the reporting of amounts for financial statement purposes and income tax purposes. These differences relate primarily to different methods used for income tax reporting purposes, including for depreciation and amortization, warranty and vacation accruals, and deductions related to allowances for doubtful accounts receivable and inventory reserves. Our provision for income taxes included current federal and state income tax expense, as well as deferred federal and state income tax expense.

The effective tax rate for the three months ended March 31, 2019 was a benefit of 189.7%, compared to a benefit of 97.1% for the three months ended March 31, 2018. The primary driver of the change in our effective tax rate was attributable to an increase in the tax benefits related to share-based compensation proportionate to pre-tax book income as compared to the prior year's reporting period. We recorded an income tax benefit of $3.1 million and $1.7 million for the three months ended March 31, 2019 and 2018, respectively.

We recognize the financial statement benefit of a tax position only after determining that the relevant tax authority is more-likely-than-not to sustain the position following an audit. For tax positions meeting the more-likely-than-not threshold, the amount recognized in the condensed consolidated financial statements is the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement with the relevant tax authority. As of March 31, 2019 we had an unrecognized tax benefit classified as a non-current liability.

We are not currently under examination in any jurisdiction. In the event of any future tax assessments, we have elected to record the income taxes and any related interest and penalties as income tax expense on our statement of operations.

Note 14. Net Income Per Share

The following table sets forth the computation of our basic and diluted net income (loss) per share attributable to common stockholders:

(In thousands, except share and per share data)	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Net income (loss)	$ 1,472	$ (50)
Weighted-average shares outstanding	18,746,751	17,996,672
Effect of restricted stock units, common stock options, and employee stock purchase plan shares	833,096	—
Weighted-average shares used to compute diluted net income per share	19,579,847	17,996,672
Net income per share - Basic	$ 0.08	$ 0.00
Net income per share - Diluted	$ 0.08	$ 0.00

The following common stock equivalents were excluded from the computation of diluted net income per share for the periods presented because including them would have been anti-dilutive:

	Three Months Ended March 31, 2019	Three Months Ended March 31, 2018
Restricted stock units	42,691	395,046
Common stock options	165,638	1,445,089
Employee stock purchase plan	—	68,114
Total	208,329	1,908,249

Note 15. Fair Value Measurements

We determine the fair value of our assets and liabilities based on the exchange price that would be received for an asset or paid to transfer a liability (exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value maximize the use of observable inputs and minimize the use of unobservable inputs. We use a fair value hierarchy with three levels of inputs, of which the first two are considered observable and the last unobservable, to measure fair value. The fair value hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities (Level 1). The next highest priority is based on quoted prices for similar assets or liabilities in active markets or quoted prices for identical or similar assets or liabilities in non-active markets or other observable inputs (Level 2). The lowest priority is given to unobservable inputs (Level 3).

The following provides information regarding fair value measurements for our cash equivalents and marketable securities as of March 31, 2019 and December 31, 2018 according to the three-level fair value hierarchy:

(In thousands)	At March 31, 2019 Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Recurring Fair Value Measurements:				
Money market mutual funds	$ 7,055	$ —	$ —	$ 7,055
U.S. government and agency obligations	16,402	999	—	17,401
Corporate debt securities	—	3,983	—	3,983
Total	$ 23,457	$ 4,982	$ —	$ 28,439

(In thousands)	At December 31, 2018 Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total
Recurring Fair Value Measurements:				
Money market mutual funds	$ 2,447	$ —	$ —	$ 2,447
U.S. government and agency obligations	16,326	2,994	—	19,320
Corporate debt securities	—	6,466	—	6,466
Total	$ 18,773	$ 9,460	$ —	$ 28,233

During the three months ended March 31, 2019, there were no transfers within the three-level hierarchy. A significant transfer is recognized when the inputs used to value a security have been changed, which merits a transfer between the disclosed levels of the valuation hierarchy.

The fair values for our money market mutual funds, U.S. government and agency obligations and corporate debt securities are determined based on valuations provided by external investment managers who obtain them from a variety of industry standard data providers.

The carrying amounts of financial instruments such as cash equivalents, accounts receivable, other assets, accounts payable, accrued expenses and other liabilities approximate their related fair values due to the short-term maturities of these items. Non-financial assets, such as equipment and leasehold improvements, and intangible assets are subject to non-recurring fair value measurements if they are deemed impaired. As of December 31, 2018, we re-measured the value of our intangible assets related to the Actitouch product line to their fair value, which was deemed to be $0 using level 3 measurements. We had no re-measurements of non-financial assets to fair value in the three months ended March 31, 2019.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and the accompanying notes thereto included elsewhere in this report.

Overview

We are a medical technology company that develops and provides innovative medical devices for the treatment of chronic diseases. Our mission is to help people suffering from chronic diseases live better and care for themselves at home. We focus our efforts on advancing the standard of care in treating chronic diseases in the home setting to improve patient outcomes and quality of life and help control rising healthcare expenditures. Our initial area of therapeutic focus is vascular disease, with a goal of advancing the standard of care in treating lymphedema and chronic venous insufficiency. We possess a unique, scalable platform to deliver at-home healthcare solutions throughout the United States. This evolving home care delivery model is recognized by policy-makers and insurance payers as a key for controlling rising healthcare costs. Our solutions deliver cost-effective, clinically proven, long-term treatment for people with these chronic diseases.

Our proprietary products are the Flexitouch, Entre, and Actitouch systems. A predecessor to our Flexitouch system received 510(k) clearance from the U.S. Food and Drug Administration (the "FDA") in July 2002, and we introduced the system to address the many limitations of self-administered home-based manual lymphatic drainage therapy. We began selling our more advanced Flexitouch system after receiving 510(k) clearance from the FDA in October 2006. In September 2016, we received 510(k) clearance from the FDA for the Flexitouch system in treating lymphedema of the head and neck. In June 2017, we announced that we received 510(k) clearance from the FDA for the Flexitouch Plus, the third-generation version of our Flexitouch system. We derive the vast majority of our revenues from our Flexitouch system. For each of the three months ended March 31, 2019 and 2018, sales and rentals of our Flexitouch system represented 91% of our revenues.

In September 2012, we acquired our second proprietary product, the Actitouch system. The system received 510(k) clearance from the FDA in June 2013 and we began selling the product in September 2013 to address the many limitations of multilayered bandages that are worn by patients suffering from venous leg ulcers. We also introduced our Entre system in the United States in February 2013. The Entre system is sold to patients who need a more basic pump or who do not yet qualify for insurance reimbursement for an advanced compression device such as our Flexitouch system. For each of the three months ended March 31, 2019 and 2018, sales and rentals of our Entre and Actitouch systems combined represented 9% of our revenues. During fiscal year 2018, we recorded a $2.5 million non-cash impairment charge to fully impair the inventory and intangible assets related to our Actitouch system, and we intend to discontinue this product line in the second half of 2019. See Note 3 - "Summary of Significant Accounting Policies" in our Annual Report on Form 10-K for the year ended December 31, 2018 for more information regarding this impairment charge and discontinuation.

In October 2018, we licensed the intellectual property rights related to the Airwear Gradient Compression Wrap, or the Airwear wrap, in the U.S. and Canada, for use in all medical applications, including but not limited to swelling/edema and ulcers (including lymphedema and chronic venous insufficiency conditions), but excluding the use of the intellectual property in the field of prophylaxis for deep vein thrombosis. The Airwear wrap is indicated for the management of venous insufficiency, venous hypertension, venous ulcerations and lymphedema. We plan to begin selling the Airwear wrap in the second half of 2019.

To support the growth of our business, we invest heavily in our commercial infrastructure, consisting of our direct salesforce, home training resources, reimbursement capabilities and clinical expertise. We market our products in the United States using a direct-to-patient and -provider model. Our direct salesforce has grown to a team of over 210 employees as of March 31, 2019, compared to over 160 employees as of March 31, 2018. This model allows us to directly approach patients and clinicians, whereby we disintermediate the traditional durable medical equipment channel, allowing us to capture both the manufacturer and distributor margins. We also utilize over 560 licensed, independent healthcare practitioners as home trainers who educate patients on the proper use of our systems. We invest substantial resources in our Reimbursement Department, which was reorganized in 2018 to improve operational efficiencies and enhance individual payer expertise, while continuing our strategic focus of payer development. The Reimbursement Department, composed of over

75 employees, now consists of our Payer Development and Reimbursement Operations groups. Our Payer Development group is composed of both strategic and analytical teams, with focus on payer decision-maker relationships and education, payer policy development and revision, payer contract negotiations, and payer data analysis. Our experienced Reimbursement Operations group is responsible for verifying patient insurance benefits, individual patient case development, prior authorization submissons, case follow-up, and appeals when necessary. We also have a clinical team, consisting of a scientific advisory board, in-house therapists and nurses, and a medical director (part-time), that serves as a resource to clinicians and patients and guides the development of clinical evidence in support of our products.

We rely on third-party contract manufacturers for the sourcing of parts, the assembly of our controllers and the manufacturing of the garments used with our systems. We conduct final assembly of the garments used with our Flexitouch system, perform quality assurance, and ship our products from our facility in Minneapolis, Minnesota.

In February 2016, the FASB issued ASU No. 2016-02, "Leases" (Topic 842), which supersedes the existing guidance for lease accounting, "Leases" (Topic 840). ASC 842 requires lessees to recognize a lease liability and a right of use asset for all leases that extend beyond one year. As a result of our change in filing status, we adopted this standard using the modified retrospective transition approach at the adoption date of January 1, 2019. This approach does not require restatement of previous periods. We completed a qualitative and quantitative assessment of our leases from both a lessee and lessor perspective. As part of our process, we elected to utilize certain practical expedients that were provided for transition relief. Accordingly, we did not reassess expired or existing contracts, lease classifications or related initial direct costs as part of our assessment process for either lessee or lessor leases. Additionally, we elected the practical expedient to treat lease and nonlease components of fixed payments due to the lessor as one, and therefore no separate allocation was required on the initial implementation date of January 1, 2019, and thereafter. The adoption of this standard, from a lessee perspective, resulted in us recording ROU operating lease assets and liabilities of approximately $3.1 million on the Condensed Consolidated Balance Sheet as of January 1, 2019, with no impact to retained earnings. In addition, we elected as an accounting policy, not to record leases with an initial term of less than 12 months. From a lessor perspective, the application of ASC 842 to our rental revenue, which was recognized as month-to-month, cancelable leases in accordance with ASC 840 through December 31, 2018, resulted in recognizing rental revenue as a sales-type lease under ASC 842 thereafter. Rental sales agreements that commenced prior to December 31, 2018, will continue to be recognized as month-to-month, cancelable leases until they are completed, as we elected the practical expedient to not reassess the lease classification for leases in existence upon adoption. As such, rental agreements commencing after January 1, 2019 were recorded as sales-type leases with the associated revenue and cost of revenue recognized on the lease commencement date and a corresponding net investment in leases on the Condensed Consolidated Balance Sheet. (See Note 10 – "Commitments and Contingencies" and Note 12 – "Revenue" for additional information and required disclosures.)

As a result of our adoption of ASC 842, our rental revenue is such that, beginning with the three months ended March 31, 2019, rental revenue, cost of rental revenue and gross profit - rental revenue are presented as line items separate from sales revenue, cost of sales revenue and gross profit - sales revenue, respectively, in our Condensed Consolidated Statements of Operations. Our adoption of ASC 842 under the modified retrospective transition approach did not require restatement of previous periods, and therefore rental revenue, cost of rental revenue and gross profit - rental revenue for the three months ended March 31, 2018 were determined under ASC 840, inclusive of rental garments, but have been presented as separate line items in this report to conform to the current year presentation.

For the three months ended March 31, 2019, we generated revenues of $37.6 million and had net income of $1.5 million, compared to revenues of $26.8 million and a net loss of $0.1 million for the three months ended March 31, 2018.

Our primary sources of capital to date have been from operating income, private placements of our capital stock, and capital raised in our initial public offering, which closed on August 2, 2016.

We operate in one segment for financial reporting purposes.

Results of Operations

Comparison of the Three Months Ended March 31, 2019 and 2018

The following table presents our results of operations for the periods indicated:

	Three Months Ended March 31,				Change	
(In thousands)	2019		2018		$	%
Condensed Consolidated Statement of Operations Data:		% of revenue		% of revenue		
Revenue						
Sales revenue	$ 30,831	82 %	$ 23,647	88 %	$ 7,184	30 %
Rental revenue	6,786	18 %	3,201	12 %	3,585	112 %
Total revenue	37,617	100 %	26,848	100 %	10,769	40 %
Cost of revenue						
Cost of sales revenue	9,412	25 %	6,409	24 %	3,003	47 %
Cost of rental revenue	1,947	5 %	900	3 %	1,047	116 %
Total cost of revenue	11,359	30 %	7,309	27 %	4,050	55 %
Gross profit						
Gross profit - sales revenue	21,419	57 %	17,238	64 %	4,181	24 %
Gross profit - rental revenue	4,839	13 %	2,301	9 %	2,538	110 %
Gross profit	26,258	70 %	19,539	73 %	6,719	34 %
Operating expenses						
Sales and marketing	17,391	47 %	12,557	48 %	4,834	38 %
Research and development	1,281	3 %	1,437	5 %	(156)	(11)%
Reimbursement, general and administrative	9,388	25 %	7,372	27 %	2,016	27 %
Total operating expenses	28,060	75 %	21,366	80 %	6,694	31 %
Loss from operations	(1,802)	(5)%	(1,827)	(7)%	25	(1)%
Other income	161	— %	91	— %	70	77 %
Loss before income taxes	(1,641)	(5)%	(1,736)	(7)%	95	(5)%
Income tax benefit	(3,113)	(8)%	(1,686)	(7)%	(1,427)	85 %
Net income (loss)	$ 1,472	3 %	$ (50)	— %	$ 1,522	N.M. %

"N.M." Not Meaningful

Revenues

Revenues increased $10.8 million, or 40%, to $37.6 million in the three months ended March 31, 2019, compared to $26.8 million in the three months ended March 31, 2018. The growth in revenues was attributable to an increase of approximately $9.6 million, or 39%, in sales and rentals of our Flexitouch system and an increase of approximately $1.2 million, or 51%, in sales and rentals of our Entre/Actitouch systems in the three months ended March 31, 2019. The increase in Flexitouch system sales and rentals was largely driven by expansion of our salesforce, growth in the Medicare channel, increased physician and patient awareness of the treatment options for lymphedema, and expanded contractual coverage with national and regional insurance payers. The increase in Entre/Actitouch systems sales and rentals was largely driven by the continued benefit from managing orders in-house and expanded contractual coverage with payers. Additionally, the adoption of ASC 842 contributed 10 percentage points to our year-over-year total revenue growth for the three months ended March 31, 2019.

Revenues from the Veterans Administration represented 20% and 23% of total revenues in the three months ended March 31, 2019 and 2018, respectively. Revenues from Medicare represented 11% and 10% of total revenues in the three months ended March 31, 2019 and 2018, respectively.

The following table summarizes our revenues by product for the three months ended March 31, 2019 and 2018, both in dollars and percentage of total revenues:

	Three Months Ended March 31,		Change	
(In thousands)	2019	2018	$	%
Revenues				
Flexitouch system	$ 34,109	$ 24,530	$ 9,579	39 %
Entre/Actitouch systems	3,508	2,318	1,190	51 %
Total	$ 37,617	$ 26,848	$ 10,769	40 %
Percentage of total revenues				
Flexitouch system	91 %	91 %		
Entre/Actitouch systems	9 %	9 %		
Total	100 %	100 %		

Our business is affected by seasonality. In the first quarter of each year, when most patients have started a new insurance year and have not yet met their annual out-of-pocket payment obligations, we experience substantially reduced demand for our products. We typically experience higher revenues in the third and fourth quarters of the year as a result of patients having paid their annual insurance deductibles in full, thereby reducing their out-of-pocket costs for our products, and because patients often spend the remaining balances in their healthcare flexible spending accounts at that time. This seasonality applies only to purchases and rentals of our products by patients covered by commercial insurance and is not relevant to Medicare, Medicaid, or the Veterans Administration, as those payers either do not have plans that have declining deductibles over the course of the plan year or do not have plans that include patient deductibles for purchases or rentals of our products.

Cost of Revenue and Gross Margin

Cost of revenue increased $4.1 million, or 55%, to $11.4 million in the three months ended March 31, 2019, compared to $7.3 million in the three months ended March 31, 2018. The increase in cost of revenue was primarily attributable to an increase in the number of Flexitouch systems sold/rented and ASC 842 leasing impact as well as additional manufacturing headcount to support increased volumes.

Sales gross margin was 70% of sales revenue in the three months ended March 31, 2019, compared to 73% of sales revenue in the three months ended March 31, 2018. Rental gross margin was 71% of rental revenue in the three months ended March 31, 2019, compared to 72% of rental revenue in the three months ended March 31, 2018. The gross margin decreases were primarily attributable to negative pricing effects related to the new large private insurer contract we entered into in July 2018, the composition of sales mix by payer and by product in comparison to the prior year, and amortization expense related to the newly licensed assets from Sun Scientific, Inc.

Sales and Marketing Expenses

Sales and marketing expenses increased $4.8 million, or 38%, to $17.4 million in the three months ended March 31, 2019, compared to $12.6 million in the three months ended March 31, 2018. The increase was primarily driven by a $3.3 million increase in personnel-related compensation expense due to increased sales and marketing headcount, including $0.5 million of incremental stock-based compensation expense. In addition, other sales and marketing expenses increased $1.5 million, driven by increased spending associated with field sales meetings, travel and entertainment, recruiting, and patient training expenses.

Research and Development Expenses

Research and development (“R&D”) expenses decreased $0.2 million, or 11%, to $1.3 million in the three months ended March 31, 2019, compared to $1.4 million in the three months ended March 31, 2018. The decrease was primarily attributable to the timing of clinical studies projects.

Reimbursement, General and Administrative Expenses

Reimbursement, general and administrative expenses increased $2.0 million, or 27%, to $9.4 million in the three months ended March 31, 2019, compared to $7.4 million in the three months ended March 31, 2018. This increase was primarily attributable to a $1.2 million increase in personnel-related compensation expense as a result of increased headcount in our reimbursement operations, payer development and corporate functions, including $0.7 million of incremental stock-based compensation expense. The increase in reimbursement, general and administrative expenses was also attributable to a $0.7 million increase in professional fees, legal expenses, facilities, and depreciation as well as $0.1 million in legal expenses specifically related to the defense of the ongoing lawsuit described in "Legal Proceedings" in this report.

Other Income, Net

Other income was $0.2 million and $0.1 million for the three months ended March 31, 2019 and 2018, respectively. The increase in other income was primarily due the accretion of discounts on purchases of marketable securities.

Income Taxes

We recorded an income tax benefit of $3.1 million and $1.7 million in the three months ended March 31, 2019 and 2018, respectively. The continued significant tax deductions related to tax benefits realized from the vesting of restricted stock units, the exercise of non-qualified stock options, and the disqualifying dispositions of incentive stock options and ESPP shares contributed to our net income for the three months ended March 31, 2019. The increase in the current period income tax benefit was due to increased tax-deductible share-based compensation activity recognized in the three months ended March 31, 2019.

Liquidity and Capital Resources

Cash Flows

At March 31, 2019, our principal sources of liquidity were cash and cash equivalents of $23.5 million, marketable securities of $21.4 million and net accounts receivable of $23.8 million, and the borrowing capacity available under our Credit Agreement.

The following table summarizes our cash flows for the periods indicated:

	Three Months Ended March 31,	
(In thousands)	2019	2018
Net cash provided by (used in):		
Operating activities	$ 1,273	$ (2,173)
Investing activities	3,725	4,568
Financing activities	(1,549)	(1,050)
Net increase in cash and cash equivalents	$ 3,449	$ 1,345

Operating Activities

Net cash provided by operating activities during the three months ended March 31, 2019 was $1.3 million, resulting from net income of $1.5 million and non-cash net income adjustments of $1.5 million, which were offset by a net increase in operating assets and liabilities of $1.7 million. The non-cash net income adjustments consisted of $2.8 million of stock-based compensation expense and $1.0 million of depreciation and amortization expense, partially offset by deferred income tax changes of $2.3 million. The uses of cash related to changes in operating assets primarily consisted of increases in net investment in leases of $3.4 million, right of use operating lease assets of $3.4 million and income taxes receivable of $1.0 million, partially offset by a decrease in accounts receivable of $2.7 million. The changes in operating liabilities consisted of increases in right of use operating lease liabilities of $3.5 million and accounts payable of $0.7 million, partially offset by a decrease in accrued payroll and related taxes of $0.6 million. These changes occurred primarily due to the adoption of ASC 842.

Net cash used in operating activities in the three months ended March 31, 2018 was $2.2 million, resulting from a net loss of $0.1 million and a net increase in operating assets and liabilities of $4.1 million, partially offset by non-cash operating expenses of $2.0 million. The changes in net operating assets and liabilities were primarilty due to a $3.6 million increase in inventories, associated with the commercial launch of our next-generation Flexitouch system; a $1.8 million decrease in accrued payroll and related taxes, driven by the payment of 2017 bonuses; and a $1.8 million increase in income taxes receivable, driven by the tax benefit associated with tax-deductible stock-based compensation activity in that period, partially offset by a $3.4 million decrease in accounts receivable. The non-cash operating expenses primarily consisted of $1.5 million of stock-based compensation and $0.5 million of depreciation and amortization of equipment, leasehold improvements and patents.

Investing Activities

Net cash provided by investing activities during the three months ended March 31, 2019 was $3.7 million, primarly consisting of $4.5 million in maturities of marketable securities partially offset by $0.7 million in purchases of product tooling and computer and manufacturing equipment, leasehold improvements and furniture and fixtures.

Net cash provided by investing activities during the three months ended March 31, 2018 was $4.6 million, consisting primarily of $5.0 million in sales and maturities of marketable securities, offset by $0.4 million in purchases of product tooling and computer and manufacturing equipment.

Financing Activities

Net cash used in financing activities during the three months ended March 31, 2019 was $1.5 million, consisting of $2.4 million in taxes paid for the net share settlement of restricted stock units, offset by proceeds from exercises of common stock options of $0.9 million.

Net cash used in financing activities during the three months ended March 31, 2018 was $1.1 million, consisting of $1.2 million in taxes paid for the net share settlement of restricted stock units, offset by proceeds from exercises of common stock options of $0.1 million.

Credit Agreement

On August 3, 2018, we entered into a credit agreement with Wells Fargo Bank, National Association, which was amended by a First Amendment dated February 12, 2019 and a Waiver and Second Amendment dated March 25, 2019 (collectively, the “Credit Agreement”), which expires on August 3, 2021. The Credit Agreement provides for a $10.0 million revolving credit facility, with the ability to increase the amount of the revolving loans available and/or add one or more term loan facilities not to exceed an incremental $25.0 million, subject to satisfaction of certain conditions. As of March 31, 2019, and the date on which we filed this report, we did not have any outstanding borrowings under the Credit Agreement.

Our obligations under the Credit Agreement are secured by a security interest in substantially all of our and our subsidiaries’ assets and are also guaranteed by our subsidiaries. The Credit Agreement contains a number of restrictions and covenants, including that we maintain compliance with a maximum leverage ratio and a minimum liquidity covenant. As of March 31, 2019, we were in compliance with all financial covenants under the Credit Agreement. For additional information on the Credit Agreement, see Note 9 – “Credit Agreement” to the condensed consolidated financial statements in this report.

Adequacy of Capital Resources

Our future capital requirements may vary significantly from those now planned and will depend on many factors, including:

- sales and marketing resources needed to further penetrate our market;
- expansion of our operations domestically and/or internationally;
- responses of competitors to our solutions and applications;
- costs associated with clinical research activities;
- costs to develop and implement new products; and
- use of capital for acquisitions or licenses, if any.

Historically, we have experienced increases in our expenditures consistent with the growth in our revenues, operations and personnel, and we anticipate that our expenditures will continue to increase as we expand our business.

We believe our cash, cash equivalents, marketable securities and cash flows from operations together with the Credit Agreement will be sufficient to meet our working capital and capital expenditure requirements for at least the next twelve months.

Inflation and changing prices did not have a material effect on our business during the three months ended March 31, 2019, and we do not expect that inflation or changing prices will materially affect our business for at least the next twelve months.

In August 2017 we filed a shelf registration statement on Form S-3 with the SEC. Under the shelf registration statement, we may offer and sell from time to time up to $200 million of common stock, preferred stock, debt securities, warrants, rights or units. The shelf registration statement also registered for resale from time to time up to 5,703,534 shares of our common stock held by the selling stockholders named therein. In September 2017 certain of the selling stockholders completed a secondary offering of 3,795,000 shares of our common stock at a public offering price of $33.00 per share. We did not receive any proceeds from the sale of the shares by the selling stockholders.

Contractual and Commercial Commitments Summary

Our contractual obligations and commercial commitments as of March 31, 2019 are summarized below:

	Payments Due By Period				
(In thousands)	**Total**	**Less Than 1 Year**	**1-3 Years**	**3-5 Years**	**More Than 5 Years**
Purchase commitments [(1)]	$ 19,505	$ 19,505	$ —	$ —	$ —
Operating lease obligations [(2)]	3,694	1,290	1,653	751	—
Future product royalties [(3)]	3	3	—	—	—
Total	$ 23,202	$ 20,798	$ 1,653	$ 751	$ —

(1) We issued purchase orders prior to March 31, 2019 totaling $19.5 million for goods that we expect to receive between April and December of 2019.

(2) We currently lease approximately 52,000 square feet of office space for our corporate headquarters in Minneapolis, Minnesota, under a lease that expires in July 2021 and 44,000 square feet of office, assembly and warehouse space at another leased facility in Minneapolis, Minnesota, under a lease that expires in February 2024. We entered into a lease in October 2018 for approximately 110,000 square feet of office space for our future corporate headquarters in Minneapolis, Minnesota, which will commence upon our move, which is expected to occur in the fourth quarter of 2019. That lease expires in February 2030. As of March 31, 2019, we have lease commitments of $19.9 millions related to our future headquarters that are not included in the table above, since we have not

yet recognized it as an operating lease. As the lessee, we are involved in providing guidance to the lessor for related improvements, however these improvements are managed and owned by the lessor. We entered into a fleet vehicle program for certain members of our field sales organization in 2016. At March 31, 2019, we had 40 vehicles under this program with current lease commitments. Furthermore, we lease office equipment from time-to-time based on our needs and these commitments are classified as operating leases.

(3) We are required to make quarterly royalty payments to a third-party for our Actitouch system revenue through August 2023. Beginning in September 2017, the payments are equal to 6% of our quarterly revenues attributable to our Actitouch system. In any year that these revenues exceed $40.0 million, we are required to pay 7% on revenues over $40.0 million and 6% on revenues of $40.0 million and under. Because our revenues attributable to our Actitouch system, and therefore the amount of royalty payments we will be required to pay in the future, are unknown, this amount only reflects royalties due associated with a portion of our 2019 Actitouch revenues.

Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, investments in special purpose entities or undisclosed borrowings or debt. Additionally, we are not a party to any derivative contracts or synthetic leases.

Recent Accounting Pronouncements

Refer to Note 3 - “Summary of Significant Accounting Policies” of our condensed consolidated financial statements contained in this report for a description of recently issued accounting pronouncements that are applicable to our business.

JOBS Act

Prior to December 31, 2018, we were an “emerging growth company” as defined by the JOBS Act. The JOBS Act provides that an emerging growth company can take advantage of the extended transition period for complying with new or revised accounting standards. This allows an emerging growth company to delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We elected to avail ourselves of this exemption prior to December 31, 2018, and as a result, our financial statements prior to that date may not have been comparable to the financial statements of issuers who are required to comply with the effective dates for new or revised accounting standards that are applicable to public companies.

Subject to certain conditions, as an emerging growth company we also were able to rely on certain of the exemptions and reduced reporting requirements of the JOBS Act, including without limitation, from providing an auditor's attestation report on our system of internal control over financial reporting pursuant to Section 404(b) of the Sarbanes-Oxley Act of 2002 and from complying with any requirement that may be adopted by the Public Company Accounting Oversight Board regarding mandatory audit firm rotation or a supplement to the auditor's report providing additional information about the audit and the financial statements, known as the auditor discussion and analysis. Because the market value of our common stock that was held by non-affiliates as of the last business day of our second fiscal quarter of 2018 exceeded $700 million, we were deemed a large accelerated filer and no longer qualify as an emerging growth company as of December 31, 2018. As a result, we no longer are able to take advantage of the extended transition period for the adoption of certain accounting standards or of the reduced disclosure and other benefits available to emerging growth companies, including our exemption from providing our auditor’s attestation on our system of internal control over financial reporting, which was included for the first time our Annual Report on Form 10-K for the year ended December 31, 2018.

Critical Accounting Policies and Estimates

A "critical accounting policy" is one that is both important to the portrayal of our financial condition and results and requires management's most subjective or complex judgments, often as a result of the need to make estimates about the effect of items that are inherently uncertain. For additional information, please see the discussion of our significant accounting policies under "Critical Accounting Policies and Significant Estimates" in Management's Discussion and Analysis of Financial Condition and Results of Operations in our Annual Report on Form 10-K for the year ended December 31, 2018.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

We are exposed to market risk from changes in interest rates, primarily related to our investment activities. The principal objectives of our investment activities are to preserve principal, provide liquidity and maximize income consistent with minimizing risk of material loss. The recorded carrying amounts of cash and cash equivalents approximate fair value due to their short maturities. Our interest income is sensitive to changes in the general level of interest rates in the United States, particularly since our investments are generally short-term in nature. Based on the nature of our short-term investments, an immediate 100 basis point change in interest rates would not have a material effect on the fair market value of our portfolio.

Inflation

Inflationary factors, such as increases in our cost of revenue, sales and marketing expenses and reimbursement expenses, may adversely affect our operating results. Although we do not believe that inflation has had a material impact on our financial condition or results of operations to date, a high rate of inflation in the future may have an adverse effect on our ability to maintain and increase our gross margin, and on our sales and marketing and reimbursement expenses as a percentage of our revenues, if the selling and rental prices of our products do not increase as much or more than these increased costs.

Credit Risk

As of March 31, 2019 and December 31, 2018, our cash, cash equivalents and marketable securities were maintained with three financial institutions in the United States.

Our accounts receivable primarily relate to revenues from the sale and rental of our products to patients in the United States. As of March 31, 2019 and 2018, our accounts receivable and net investment in leases were $27.2 million and $17.2 million, respectively. We had accounts receivable from three insurers representing approximately 30%, 14% and 8% of accounts receivable as of March 31, 2019, and we had accounts receivable from three insurance companies representing approximately 25%, 17% and 6% of accounts receivable as of March 31, 2018.

Foreign Currency Risk

Our business is conducted in U.S. dollars and international transactions have been minimal. As we begin building relationships to commercialize and distribute our products internationally, our results of operations and cash flows may become increasingly subject to changes in foreign currency exchange rates.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of our disclosure controls and procedures as of March 31, 2019. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of March 31, 2019, our Chief Executive Officer and Chief Financial Officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting, as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act, that occurred during the quarter ended March 31, 2019 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II—OTHER INFORMATION

Item 1. Legal Proceedings.

From time to time, we are subject to various claims and legal proceedings arising in the ordinary course of business. Regardless of outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

On February 13, 2019, we were served with a sealed amended complaint venued in the United States District Court in the Southern District of Texas, Houston Division, captioned *United States ex rel Veterans First Medical Supply, LLC vs. Tactile Medical Systems Technology, Inc.,* Case No. 18-2871, which had been filed on January 23, 2019. The complaint was unsealed on March 20, 2019. The complaint is a *qui tam* action on behalf of the United States brought by one of our competitors. The United States has declined to intervene in this action. The complaint alleges that we violated the Federal Anti-Kickback Statute claiming that we submitted false claims and made false statements in connection with the Medicare and Medicaid programs, and that we engaged in unlawful retaliation in violation of the Federal False Claims Act. The complaint seeks damages, statutory penalties, attorneys' fees, treble damages and costs. We filed a motion to dismiss on April 5, 2019. We believe that the allegations in the lawsuit are without merit and we intend to continue to vigorously defend against the lawsuit.

Item 1A. Risk Factors.

In addition to the other information set forth in this Quarterly Report on Form 10-Q, you should carefully consider the factors discussed in "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2018, which could materially affect our business, financial condition or future results. There have been no material changes in our risk factors from those disclosed in that report.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Recent Sales of Unregistered Securities

(a) *Issuances of Preferred Stock*

None.

(b) *Issuances of Common Stock*

None.

Use of Proceeds from Registered Securities

On August 2, 2016, we issued and sold 4,120,000 shares of our common stock in the initial public offering at a public offering price of $10.00 per share, for aggregate gross proceeds of $41.2 million. All of the shares issued and sold in the initial public offering were registered under the Securities Act of 1933, as amended, pursuant to a Registration Statement on Form S-1 (File No. 333-209115), which was declared effective by the SEC on July 27, 2016. The offering terminated on August 2, 2016.

The net offering proceeds to us, after deducting underwriting discounts of approximately $2.9 million and offering expenses paid by us totaling approximately $2.9 million, were approximately $35.4 million. No offering expenses were paid directly or indirectly to any of our directors or officers (or their associates) or persons owning 10% or more of any class of our equity securities or to any other affiliates. We also paid $8.2 million in cumulative accrued dividends to our Series A preferred stockholders from the issuance proceeds.

At March 31, 2019, the net proceeds from our initial public offering were held in a diversified portfolio of bank deposits, government money market funds, government securities (U.S. Treasury and U.S. government agency securities), and high-grade short-term corporate bonds. All investments were in compliance with our Investment Policy and are highly liquid, with liquidity and capital preservation being the primary investment objectives. There has been no material change in our planned uses of the net proceeds from those described in the Prospectus dated July 27, 2016.

Item 3. Defaults Upon Senior Securities.

Not applicable.

Item 4. Mine Safety Disclosures.

Not applicable.

Item 5. Other Information.

None.

Item 6. Exhibits.

The exhibits filed as part of this Quarterly Report on Form 10-Q are set forth on the Exhibit Index below.

EXHIBIT INDEX

Exhibit Number	Description of Exhibit	Incorporated by Reference Form	File Number	Date of Filing	Exhibit Number	Filed Herewith
3.1	Fourth Amended and Restated Certificate of Incorporation	S-1	333-209115	06/09/2016	3.1	
3.2	Amended and Restated By-laws	S-1	333-209115	05/06/2016	3.2	
10.1	First Amendment to Credit Agreement, dated as of February 12, 2019, by and among Tactile Systems Technology, Inc., the lenders party thereto and Wells Fargo Bank, National Association	10-K	001-37799	02/28/2019	10.33	
10.2	Waiver and Second Amendment to Credit Agreement, dated as of March 25, 2019, by and among Tactile Systems Technology, Inc., the lenders party thereto and Wells Fargo Bank, National Association					X
10.3	Form of Restricted Stock Unit Award Agreement under the 2016 Equity Incentive Plan (to be used for awards beginning in 2019)					X
10.4	Form of Performance Stock Unit Agreement under the 2016 Equity Incentive Plan (to be used for awards beginning in 2019)					X
10.5	Non-Employee Director Compensation Policy	10-K	001-37799	02/28/2019	10.21	
31.1	Certification of Principal Executive Officer pursuant to Rule 13a-14(a) / 15d-14(a) of the Securities Exchange Act of 1934, as amended					X
31.2	Certification of Principal Financial Officer pursuant to Rule 13a-14(a) / 15d-14(a) of the Securities Exchange Act of 1934, as amended					X
32.1	Certification of Principal Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2	Certification of Principal Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X

101.1	The following condensed consolidated financial statements from the Company's Quarterly Report on Form 10-Q for the quarter ended March 31, 2019, formatted in XBRL: (i) Balance Sheets (unaudited), (ii) Statements of Operations (unaudited), (iii) Statements of Comprehensive Income (unaudited); (iv) Statements of Stockholders' Equity (unaudited), (v) Statements of Cash Flows (unaudited), and (vi) Notes to the Condensed Consolidated Financial Statements.	X

SIGNATURES

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.

Tactile Systems Technology, Inc.

Date: May 6, 2019	By: /s/ *Brent A. Moen*
	Brent A. Moen
	Chief Financial Officer
	(Principal financial and accounting officer)

Exhibit 10.2

Execution Version

WAIVER AND SECOND AMENDMENT TO CREDIT AGREEMENT

This Waiver and Second Amendment to Credit Agreement (this "**Amendment**") is entered into as of March 25, 2019, by and among (a) Tactile Systems Technology, Inc., a Delaware corporation (dba Tactile Medical) ("**Borrower**"), (b) the Lenders who are party to this Amendment and the Lenders who may become a party to this Amendment pursuant to the terms of the Credit Agreement (defined below) (collectively, the "**Lenders**"), and (c) Wells Fargo Bank, National Association, a national banking association, as Administrative Agent for the Lenders ("**Agent**"). This Amendment is consented and agreed to by the Guarantors.

RECITALS

A. Borrower, Lenders and Agent are parties to that certain Credit Agreement dated as of August 3, 2018, as amended by that certain First Amendment to Credit Agreement dated February 12, 2019 (as the same may be further amended, restated or modified from time to time, the "**Loan Agreement**"). Capitalized terms used but not defined in this Amendment have the meanings given to such terms in the Loan Agreement.

B. Borrower has requested that Lenders and Agent permit certain amendments and modifications to the Loan Agreement.

C. Lenders and Agent have agreed to such modifications, but only upon the terms and conditions outlined in this Amendment.

TERMS OF AGREEMENT

In consideration of the mutual covenants herein, and for other good and valuable consideration, the receipt and sufficiency of which are acknowledged, Borrower, Lenders and Agent hereby agree as follows:

1. Waiver of Certain Defaults.

(a) The Borrower acknowledges that it failed to comply with Section 8.1(c) of the Credit Agreement by failing to provide, within sixty (60) days after the end of Fiscal Year 2018, a business plan and operating and capital budget of Borrower and its Subsidiaries for the ensuing three fiscal years (the "Current Default").

(b) Upon the date on which this Amendment becomes effective and subject to the other terms and conditions of this Amendment, Agent and Lenders waive the Current Default (the "Waived Defaults").

(c) The waiver set forth in subsection (b) above is limited to the express terms thereof, and nothing herein shall be deemed a waiver by Agent or Lenders with respect to any other term, condition, representation, or covenant applicable to the Borrower under the Credit Agreement or any of the other agreements, documents, or instruments executed and delivered in connection therewith, or of the covenants described therein. The waiver set forth herein shall not be deemed to be a course of action upon which the Borrower may rely in the future, and the Borrower hereby expressly waives any claim to such effect. Agent and Lenders reserve the right to exercise any rights and remedies available to them in connection with any present or future Events of Default with respect to the Credit Agreement or any other provision of any Loan Document that do not relate to or result from the Waived Defaults.

2. Amendment and Restatement of Section 8.1(c). Section 8.1(c) of the Loan Agreement is amended and restated in its entirety as follows:

(c) Annual Business Plan and Budget. As soon as practicable and in any event within sixty (60) days after the end of each Fiscal Year, a business plan and operating and capital budget of the Borrower and its Subsidiaries for the ensuing one fiscal year, such plan to be prepared in accordance with GAAP and to include, on a quarterly basis, the following: a quarterly operating and capital budget, a projected income statement, statement of cash flows and balance sheet, calculations demonstrating projected compliance with the financial covenants set forth in Section 9.15, accompanied by a certificate from a Responsible Officer of the Borrower to the effect that such budget contains good faith estimates (utilizing assumptions believed to be reasonable at the time of delivery of such budget) of the financial condition and operations of the Borrower and its Subsidiaries for such period.

3. Representations and Warranties. Borrower represents and warrants as follows:

(a) All warranties and representations made under the Loan Agreement and the other Loan Documents are true and correct in all material respects as of the date hereof (without duplication of any materiality qualifier contained therein), except to the extent such representation or warranty expressly relates to an earlier date (in which case, such representations and warranties were true and correct in all material respects (without duplication of any materiality qualifier contained therein) as of such earlier date).

(b) The execution and delivery by Borrower and Guarantor of this Amendment (i) are and will be within Borrower's and Guarantor's organizational powers; (ii) have been authorized by all necessary organizational action; (iii) are not and will not require any Governmental Approval or violate any Applicable Law relating to any Credit Party or any Subsidiary thereof where the failure to obtain such Governmental Approval or such violation could reasonably be expected to have a Material Adverse Effect; (iv) conflict with, result in a breach of or constitute a default under any indenture, agreement or other instrument evidencing Indebtedness or a payment obligation in excess of the Threshold Amount to which such Person is a party or by which any of its properties may be bound or any Governmental Approval relating to such Person, which could, individually or in the aggregate, reasonably be expected to have a Material Adverse Effect; or (v) result in or require the creation or imposition of any Lien upon or with respect to any property now owned or hereafter acquired by such Person other than Permitted Liens.

(c) This Amendment will be valid, binding and enforceable against Borrower and Guarantor in accordance with its respective terms.

(d) Other than with respect to the Waived Defaults, no Default or Event of Default has occurred under the Loan Agreement or any of the other Loan Documents.

4. Guaranties. All guaranties of the Obligations remain in full force and effect, and all Guarantors hereby (a) consent to the modifications and changes in terms to the Loan Agreement described herein; and (b) reaffirm their guaranty obligations described in such guaranties.

5. Release and Waiver of Claims. For purposes of this section, the term Lenders and Agents specifically include each of Lender's and Agent's predecessors, successors, affiliates, and all of their past, present and future officers, trustees, directors, members, agents, contractors, employees, consultants, attorneys, assigns, insurers, stockholders, and representatives, and each of them (whether or not any of the same were acting within or without the scope of employment or engagement). The release and waiver of claims of this section is to be construed broadly in favor of Lenders and Agent and against Borrower and Guarantor. Borrower and Guarantor hereby jointly and severally affirm that they do not have any defense, claim, offset, counterclaim or other claim or action (whether known or unknown) against Lenders or Agent including, but not limited to, with respect to the Loans, the Loan Agreement or the Loan Documents, or arising out of negotiations prior to and/or contemporaneous with the execution of this Amendment, and that even if such claim, action, defense, offset or counterclaim exists or might exist on the date hereof (whether known or unknown), Borrower and Guarantor hereby knowingly and jointly and severally forever waive, release and relinquish the same. Borrower and Guarantor acknowledge that the relationship between Borrower and Guarantor, on the one hand, and Lenders and Agent, on the other hand, has been solely a borrower-lender relationship, that Lenders and Agent have not exercised control over Borrower, Guarantor or any of their respective operations, and that Borrower and Guarantor are not acting under any duress or coercion in connection with the execution of this Amendment. Borrower and Guarantor represent and warrant that they have obtained the advice of independent legal counsel, or have had the opportunity to obtain their own legal counsel and have knowingly declined to obtain such legal counsel, with respect to their execution of this Amendment and the matters set forth herein.

6. Effectiveness of Prior Documents. Except as specifically amended hereby, the Loan Agreement and the other Loan Documents shall remain in full force and effect in accordance with their respective terms. All covenants, warranties and representations contained in the Loan Agreement and the other Loan Documents are hereby reconfirmed as of the date hereof. All Collateral previously provided to secure the Loan Agreement and the Loan Documents continues as security, and Borrower and Guarantor reaffirm all of their obligations under any Loan Document to which it is a party. This is an amendment, not a novation.

7. Reimbursement of Agent's Expenses. Borrower hereby agrees to reimburse Agent for all reasonable and documented out of pocket costs and expenses relating to this Amendment. Borrower hereby authorizes Agent, at its option, to debit any account of Borrower held with the Lenders for the payment of such fees, costs and expenses.

8. No Waiver of Defaults; Warranties. The execution of this Amendment shall not be deemed to be a waiver of any Default or Event of Default under the Loan Agreement or Loan Documents, whether or not known and whether or not existing on the date of this Amendment. Lenders and Agent expressly reserve all of their rights and remedies under the Loan Agreement and Loan Documents with respect to any existing or future Defaults or Events of Default under the Loan Agreement or other Loan Documents, including this Amendment. All agreements, representations and warranties made herein shall survive the execution of this Amendment.

9. Counterparts. This Amendment may be signed in any number of counterparts, each of which shall be considered an original, but when taken together shall constitute one document.

10. Final Expression. This written Amendment is a final expression of the agreement between Lenders, Agent, Borrower and Guarantor relating to the subject matter hereof, and this written agreement may not be contradicted by evidence of any alleged oral agreement.

11. Governing Law. The governing law, submission to jurisdiction, waiver of venue, service of process and waiver of jury trial provisions set forth in Sections 12.5 and 12.6 of the Loan Agreement are incorporated herein by reference and apply to this Amendment.

[*Signature Page to Follow*]

IN WITNESS WHEREOF, the parties hereto have duly executed this Amendment as of the day and year first above written.

BORROWER:

TACTILE SYSTEMS TECHNOLOGY, INC.

By: /s/ Brent Moen
Name: Brent Moen
Title: CFO

Consented and Agreed to By:

GUARANTOR:

SWELLING SOLUTIONS, INC.

By: /s/ Brent Moen
Name: Brent Moen
Title: CFO

[Borrower and Guarantor Signature Page to Waiver and Second Amendment to Credit Agreement]

AGENT AND LENDERS:

WELLS FARGO BANK, NATIONAL ASSOCIATION, as Administrative Agent, Swingline Lender, Issuing Lender and Lender

By: /s/ Monique Dubisky
Name: Monique Dubisky
Title: Director

Exhibit 10.3

TACTILE SYSTEMS TECHNOLOGY, INC.
2016 EQUITY INCENTIVE PLAN

Restricted Stock Unit Award Agreement

Tactile Systems Technology, Inc. (the "Company"), pursuant to its 2016 Equity Incentive Plan (the "Plan"), hereby grants an award of Restricted Stock Units to you, the Participant named below. The terms and conditions of this Award are set forth in this Restricted Stock Unit Award Agreement (the "Agreement"), consisting of this cover page and the Terms and Conditions on the following pages, and in the Plan document, a copy of which has been provided to you. Any capitalized term that is not defined in this Agreement shall have the meaning set forth in the Plan as it currently exists or as it is amended in the future.

Name:

Grant Date:

Number of Restricted Stock Units:

Vesting Schedule:

By signing below or otherwise evidencing your acceptance of this Agreement in a manner approved by the Company, you agree to all of the terms and conditions contained in this Agreement and in the Plan document. You acknowledge that you have received and reviewed these documents and that they set forth the entire agreement between you and the Company regarding the grant to you of the number of Restricted Stock Units specified in the table above.

[SIGNATURE]

____
Chief Executive Officer

Tactile Systems Technology, Inc.
2016 Equity Incentive Plan
Restricted Stock Unit Award Agreement

Terms and Conditions

1. **Grant of Restricted Stock Units**. The Company hereby confirms the grant to you, as of the Grant Date and subject to the terms and conditions in this Agreement and the Plan, of the number of Restricted Stock Units specified on the cover page of this Agreement (the "Units"). Each Unit represents the right to receive one Share of the Company's common stock. The Units granted to you will be credited to an account in your name maintained by the Company. This account shall be unfunded and maintained for book-keeping purposes only, with the Units simply representing an unfunded and unsecured obligation of the Company.

2. **Restrictions Applicable to Units**. Neither this Award nor the Units subject to this Award may be sold, assigned, transferred, exchanged or encumbered other than by will or the laws of descent and distribution. Any attempted transfer in violation of this Section 2 shall be of no effect and shall result in the forfeiture of all Units. The Units and your right to receive Shares in settlement of the Units under this Agreement shall be subject to forfeiture as provided in Section 4 until satisfaction of the vesting conditions set forth in Section 3.

3. **Vesting of Units**.

(a) Scheduled Vesting. If you remain a Service Provider continuously from the Grant Date specified on the cover page of this Agreement, then the Units will vest in the numbers and on the dates specified in the Vesting Schedule on the cover page of this Agreement.

(b) Accelerated Vesting. Notwithstanding Section 3(a):

(1) *Death or Disability*. If your Service terminates prior to the final scheduled vesting date due to your death or Disability, all of the unvested Units shall vest as of such termination date.

(2) *Change in Control*. If and to the extent this Award is continued, assumed or replaced in connection with a Change in Control, and if within one year after the Change in Control you experience an involuntary termination of Service for reasons other than Cause, or you terminate your Service for Good Reason (as defined below), then all of the unvested Units shall vest as of such termination date. In addition, vesting of the Units may be accelerated during the term of the Award under the circumstances described in Sections 12(b) and 12(c) of the Plan.

(3) *Definition of "Good Reason*." "Good Reason" shall, if you have an employment agreement with the Company, have the meaning set forth in your employment agreement. If you do not have an employment agreement with the Company, "Good Reason" means the existence of one or more of the following conditions without your written consent, so long as you provided written notice to the Company of the existence of the condition not later than 90 days after the initial existence of the condition, the condition has not been remedied by the Company within

30 days after its receipt of such notice and your Service terminates no later than 130 days after the condition's initial occurrence: (i) any material, adverse change in your duties, responsibilities, or authority; (ii) a material reduction in your base salary or bonus opportunity that is not part of a general reduction applicable to employees in the same classification or grade as you; or (iii) a geographical relocation of your principal office location by more than 50 miles.

4. **Effect of Termination of Service**. Except as otherwise provided in accordance with Section 3(b), if you cease to be a Service Provider, you will forfeit all unvested Units.

5. **Settlement of Units**. After any Units vest pursuant to Section 3, the Company shall, as soon as practicable (but no later than March 15 of the year following the calendar year in which such Units vest), cause to be issued and delivered to you, or to your designated beneficiary or estate in the event of your death, one Share in payment and settlement of each vested Unit. Delivery of the Shares shall be effected by the issuance of a stock certificate to you, by an appropriate entry in the stock register maintained by the Company's transfer agent with a notice of issuance provided to you, or by the electronic delivery of the Shares to a brokerage account you designate, and shall be subject to the tax withholding provisions of Section 6 and compliance with all applicable legal requirements as provided in Section 17(c) of the Plan, and shall be in complete satisfaction and settlement of such vested Units.

6. **Tax Consequences and Withholding**. No Shares will be delivered to you in settlement of vested Units unless you have made arrangements acceptable to the Company for payment of any federal, state, local or foreign withholding taxes that may be due as a result of the delivery of the Shares. You hereby authorize the Company (or any Affiliate) to withhold from payroll or other amounts payable to you any sums required to satisfy such withholding tax obligations, and otherwise agree to satisfy such obligations in accordance with the provisions of Section 14 of the Plan.

7. **No Shareholder Rights**. The Units subject to this Award do not entitle you to any rights of a shareholder of the Company's common stock. You will not have any of the rights of a shareholder of the Company in connection with the grant of Units subject to this Agreement unless and until Shares are issued to you upon settlement of the Units as provided in Section 5.

8. **Governing Plan Document**. This Agreement and the Award are subject to all the provisions of the Plan, and to all interpretations, rules and regulations which may, from time to time, be adopted and promulgated by the Committee pursuant to the Plan. If there is any conflict between the provisions of this Agreement and the Plan, the provisions of the Plan will govern.

9. **Choice of Law**. This Agreement will be interpreted and enforced under the laws of the state of Delaware (without regard to its conflicts or choice of law principles).

10. **Binding Effect**. This Agreement will be binding in all respects on your heirs, representatives, successors and assigns, and on the successors and assigns of the Company.

11. **Section 409A of the Code**. The award of Units as provided in this Agreement and any issuance of Shares or payment pursuant to this Agreement are intended to be exempt from Section 409A of the Code under the short-term deferral exception specified in Treas. Reg. § 1.409A-l(b)(4).

12. **Compensation Recovery Policy**. To the extent that any compensation paid or payable pursuant to this Agreement is considered "incentive-based compensation" within the meaning and

subject to the requirements of Section 10D of the Exchange Act, such compensation shall be subject to potential forfeiture or recovery by the Company in accordance with any compensation recovery policy adopted by the Board or any committee thereof in response to the requirements of Section 10D of the Exchange Act and any implementing rules and regulations thereunder adopted by the Securities and Exchange Commission or any national securities exchange on which the Company's common stock is then listed. This Agreement may be unilaterally amended by the Company to comply with any such compensation recovery policy.

13. **Other Agreements.** You agree that in connection with the settlement of vested Units, you will execute such documents as may be necessary to become a party to any stockholder, voting or similar agreements as the Company may require.

14. **Restrictive Legends.** The Company may place a legend or legends on any certificate representing Shares issued in settlement of vested Units summarizing transfer and other restrictions to which the Shares may be subject under applicable securities laws, other provisions of this Agreement, or other agreements contemplated by Section 13 of this Agreement. You agree that in order to ensure compliance with the restrictions referred to in this Agreement, the Company may issue appropriate "stop transfer" instructions to its transfer agent.

15. **Electronic Delivery and Acceptance**. The Company may deliver any documents related to this Restricted Stock Unit Award by electronic means and request your acceptance of this Agreement by electronic means. You hereby consent to receive all applicable documentation by electronic delivery and to participate in the Plan through an on-line (and/or voice activated) system established and maintained by the Company or the Company's third-party stock plan administrator.

By signing the cover page of this Agreement or otherwise accepting this Agreement in a manner approved by the Company, you agree to all the terms and conditions described above and in the Plan document.

Exhibit 10.4

TACTILE SYSTEMS TECHNOLOGY, INC.
2016 EQUITY INCENTIVE PLAN

Performance Stock Unit Agreement

Tactile Systems Technology, Inc. (the "Company"), pursuant to its 2016 Equity Incentive Plan (the "Plan"), hereby grants an award of Performance Stock Units to you, the Participant named below. The terms and conditions of this Award are set forth in this Performance Stock Unit Agreement (the "Agreement"), consisting of this cover page, the Terms and Conditions on the following pages and the attached Exhibit A, and in the Plan document, a copy of which has been provided to you. Any capitalized term that is used but not defined in this Agreement shall have the meaning assigned to it in the Plan as it currently exists or as it is amended in the future.

Name of Participant:	
Target Number of Performance Stock Units:	
Maximum Number of Performance Stock Units:	
Grant Date:	
Performance Period:	
Vesting Schedule:	The number of Units determined in accordance with Exhibit A to have been earned during the Performance Period will vest on the dates specified in Section 4(a) of the Award Terms and Conditions.
Performance Goals:	See Exhibit A

By signing below or otherwise evidencing your acceptance of this Agreement in a manner approved by the Company, you agree to all of the terms and conditions contained in this Agreement and in the Plan document and acknowledge that you have received and reviewed these documents.

PARTICIPANT:	TACTILE SYSTEMS TECHNOLOGY, INC.
	By:
	Title:

Tactile Systems Technology, Inc.
2016 Equity Incentive Plan
Performance Stock Unit Agreement

Terms and Conditions

1. **Award of Performance Stock Units.** The Company hereby confirms the grant to you, as of the Grant Date and subject to the terms and conditions of this Agreement and the Plan, of an award of Performance Stock Units (the "Units") in an amount initially equal to the Target Number of Performance Stock Units (the "Target Number of Units") specified on the cover page of this Agreement. The number of Units that may actually be earned and become eligible to vest pursuant to this Award can be between [ ]% and [ ]% of the Target Number of Units, but may not exceed the Maximum Number of Performance Stock Units specified on the cover page of this Agreement. Each Unit that is earned as a result of the performance goals specified in Exhibit A to this Agreement having been satisfied and which thereafter vests represents the right to receive one Share of the Company's common stock. Prior to their settlement or forfeiture in accordance with the terms of this Agreement, the Units granted to you will be credited to a performance stock unit account in your name maintained by the Company. This account will be unfunded and maintained for book-keeping purposes only, with the Units simply representing an unfunded and unsecured contingent obligation of the Company.

2. **Restrictions Applicable to Units.** Neither this Award nor the Units subject to this Award may be sold, assigned, transferred, exchanged or encumbered other than by will or the law of descent and distribution. Any attempted transfer in violation of this Section 2 shall be void and without effect. The Units and your right to receive Shares in settlement of any Units under this Agreement shall be subject to forfeiture except to extent the Units have been earned and thereafter vest as provided in Sections 4 and 5.

3. **No Shareholder Rights**. The Units subject to this Award do not entitle you to any rights of a holder of the Company's common stock. You will not have any of the rights of a shareholder of the Company in connection with any Units granted or earned pursuant to this Agreement unless and until Shares are issued to you in settlement of earned and vested Units as provided in Section 5.

4. **Vesting and Forfeiture of Units.** The Units shall vest at the earliest of the following times and to the degree specified.

(a) Scheduled Vesting. Subject to Sections 4(b)-(d), the number of Units that have been earned during the Performance Period, as determined by the Committee in accordance with Exhibit A (the "Earned Units"), will vest on the [Initial Vesting Date] [and the Final Vesting Date] in the amounts described in this section, so long as your Service has been continuous from the Grant Date to each applicable vesting date. For these purposes, the ["Initial Vesting Date" means the date the Committee certifies (i) the degree to which the performance goals for the Performance Period have been satisfied, and (ii) the number of Units that have been earned during the Performance Period as determined in accordance with Exhibit A, which certification shall occur no later than March 15 of the calendar year immediately following the calendar year during which the Performance Period ended]. The ["Final Vesting Date"] means [ ]. The following table summarizes the percentage of the Earned Units that will vest on the applicable vesting dates:

	Vesting Date	% of the Earned Units that Vest

(b) Disability. If your Service terminates by reason of your Disability prior to the Initial Vesting Date, then you will be entitled to have vest on the Initial Vesting Date a pro rata portion of the Earned Units (had your Service been continuous until the Initial Vesting Date). The pro rata portion shall be determined by multiplying the Earned Units by a fraction whose numerator is the number of days during the Performance Period prior to your Service termination date and whose denominator is the number of days in the Performance Period. If your Service terminates by reason of your Disability after the Initial Vesting Date but prior to the Final Vesting Date, then you will be entitled to have vest on the date your Service terminates all unvested Earned Units.

(c) Death. If your Service terminates by reason of your death prior to the Initial Vesting Date, then you will be entitled to have vest on the date your Service terminates a pro rata portion of the Target Number of Units specified on the cover page of this Agreement. The pro rata portion shall be determined by multiplying the Target Number of Units by a fraction whose numerator is the number of days during the Performance Period prior to your Service termination date and whose denominator is the number of days in the Performance Period. If your Service terminates by reason of your death after the Initial Vesting Date but prior to the Final Vesting Date, then you will be entitled to have vest on the date your Service terminates all unvested Earned Units.

(d) Change in Control. If and to the extent this Award is continued, assumed or replaced in connection with a Change in Control, and if within one year after the Change in Control you experience an involuntary termination of Service for reasons other than Cause, or you terminate your Service for Good Reason (as defined below), then as of such termination date a number of Units equal to following shall vest: (i) the Target Number of Units or, if the Performance Period has ended, the Earned Units, minus (ii) the number of Units that vested prior to such termination date.

If this Award is not continued, assumed or replaced in connection with a Change in Control and vesting of the Units is being accelerated in accordance with Sections 12(b) and 12(c) of the Plan, then in such case the number of Units that may be accelerated shall be the Target Number of Units (or if the Performance Period has ended, the Earned Units) minus the number of Units that vested prior to the date of the Change in Control.

"Good Reason" shall, if you have an employment agreement with the Company or are subject to a Company severance policy, have the meaning set forth in your employment agreement or such severance policy. In all other cases, "Good Reason" means the existence of one or more of the following conditions without your written consent, so long as you provided written notice to the Company of the existence of the condition not later than 90 days after the initial existence of the condition, the condition has not been remedied by the Company within 30 days after its receipt of such notice and your Service terminates no later than 130 days after the condition's initial occurrence: (i) any material, adverse change in your duties, responsibilities, or authority; (ii) a material reduction in your base salary or bonus opportunity that is not part of a general reduction applicable to employees in the same classification or grade as you; or (iii) a geographical relocation of your principal office location by more than 50 miles.

(e) Forfeiture of Unvested Units. To the extent any of Sections 4(a) through (d) is applicable to this Award, any Units that do not vest on the applicable vesting date as provided therein shall immediately be forfeited. If your Service terminates prior to the Final Vesting Date under circumstances other than as set forth in Sections 4(b) through (d), all unvested Units shall be forfeited immediately after the termination of your Service.

5. **Settlement of Units**. Subject to Section 7 below, as soon as practicable after any date on which Units vest (but no later than the 15th day of the third calendar month following the applicable vesting date), the Company shall cause to be issued and delivered to you (or to your personal representative or your designated beneficiary or estate in the event of your death, as applicable) one Share in payment and

settlement of each vested Unit. Delivery of the Shares shall be effected by the issuance of a stock certificate to you, by an appropriate entry in the stock register maintained by the Company's transfer agent with a notice of issuance provided to you, or by the electronic delivery of the Shares to a brokerage account you designate, and shall be subject to the tax withholding provisions of Section 6 and compliance with all applicable legal requirements as provided in Section 17(c) of the Plan, and shall be in complete satisfaction and settlement of such vested Units. If the Units that vest include a fractional Unit, the Company shall round the number of vested Units to the nearest whole Unit prior to issuance of Shares as provided herein.

6. **Tax Consequences and Withholding**. No Shares will be delivered to you in settlement of vested Units unless you have made arrangements acceptable to the Company for payment of any federal, state, local or foreign withholding taxes that may be due as a result of the delivery of the Shares. You hereby authorize the Company (or any Affiliate) to withhold from payroll or other amounts payable to you any sums required to satisfy such withholding tax obligations, and otherwise agree to satisfy such obligations in accordance with the provisions of Section 14 of the Plan.

7. **Compensation Recovery Policy**. To the extent that this Award and any compensation associated therewith is considered "incentive-based compensation" within the meaning and subject to the requirements of Section 10D of the Exchange Act, this Award and any compensation associated therewith shall be subject to potential forfeiture or recovery by the Company in accordance with any compensation recovery policy adopted by the Board or the Committee in response to the requirements of Section 10D of the Exchange Act and any implementing rules and regulations thereunder adopted by the Securities and Exchange Commission or any national securities exchange on which the Company's Shares are then listed. This Agreement may be unilaterally amended by the Committee to comply with any such compensation recovery policy.

8. **Additional Provisions**.

(a) Governing Plan Document. This Agreement and the Award are subject to all the provisions of the Plan, and to all interpretations, rules and regulations which may, from time to time, be adopted and promulgated by the Committee pursuant to the Plan. If there is any conflict between the provisions of this Agreement and the Plan, the provisions of the Plan will govern.

(b) Choice of Law. This Agreement shall be interpreted and enforced under the laws of the State of Delaware (without regard to its conflicts or choice of law principles).

(c) Binding Effect. This Agreement will be binding in all respects on your heirs, representatives, successors and assigns, and on the successors and assigns of the Company.

(d) Section 409A of the Code. The award of Units as provided in this Agreement and any issuance of Shares or payment pursuant to this Agreement are intended to be exempt from Section 409A of the Code under the short-term deferral exception specified in Treas. Reg. § 1.409A-l(b)(4).

(e) Electronic Delivery and Acceptance. The Company may deliver any documents related to this Award by electronic means and request your acceptance of this Agreement by electronic means. You hereby consent to receive all applicable documentation by electronic delivery and to participate in the Plan through an on-line (and/or voice activated) system established and maintained by the Company or the Company's third-party stock plan administrator.

By signing the cover page of this Agreement or otherwise accepting this Agreement in a manner approved by the Company, you agree to all the terms and conditions described above and in the Plan document.

Exhibit A

TACTILE SYSTEMS TECHNOLOGY, INC.
Performance Stock Unit Agreement
Performance Goals and Determination of Earned Units

Participant:

Grant Date:

Target Number of Units:

Performance Period:

Determination of Earned Units:

Exhibit 31.1

CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Gerald R. Mattys, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Tactile Systems Technology, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Gerald R. Mattys

Gerald R. Mattys

Chief Executive Officer

Date: May 6, 2019

Exhibit 31.2

CERTIFICATION PURSUANT TO RULE 13a-14(a)/15d-14(a) OF THE SECURITIES EXCHANGE ACT OF 1934, AS ADOPTED PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Brent A. Moen, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Tactile Systems Technology, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

    a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

    b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

    c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

    d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

    a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

    b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Brent A. Moen
Brent A. Moen
Chief Financial Officer

Date: May 6, 2019

Exhibit 32.1

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Tactile Systems Technology, Inc. (the "Company") for the period ended March 31, 2019, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), the undersigned, Gerald R. Mattys, Chief Executive Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Gerald R. Mattys
Gerald R. Mattys
Chief Executive Officer

Date: May 6, 2019

Exhibit 32.2

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report on Form 10-Q of Tactile Systems Technology, Inc. (the “Company”) for the period ended March 31, 2019, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), the undersigned, Brent A. Moen, Chief Financial Officer of the Company, hereby certifies, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that to his knowledge:

(1) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Brent A. Moen
Brent A. Moen
Chief Financial Officer

Date: May 6, 2019