

NANOGEN INC
Form 424B5
August 27, 2007
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Filed pursuant to Rule 424(b)(5)

Registration File No.: 333-144880

Prospectus Supplement

(To prospectus dated August 2, 2007)

NANOGEN, INC.

\$20,000,000

6.25% Senior Convertible Notes Due 2010,

Warrants to Purchase Common Stock,

Common Stock Issuable upon Conversion of such Notes, and

Common Stock Issuable upon Exercise of such Warrants

We are offering \$20.0 million in aggregate principal amount of our unsecured senior convertible notes, or the Notes, convertible initially into an aggregate of 15,748,030 shares of our common stock. In addition, we are issuing Series A Warrants, Series B Warrants and Series C Warrants to purchase shares of our common stock, or the Warrants, exercisable initially into an aggregate of 11,023,621 shares of our common stock, and may become exercisable for an additional 6,299,212 shares of our common stock. We are also offering shares of our common stock issuable upon conversion of the Notes and exercise of the Warrants. This prospectus also relates to the potential issuance by us of shares of common stock to the holders of Notes in payment of interest on the Notes. For each \$100 of Notes purchased by an investor, the investor also will receive a Series A Warrant to purchase 31.49606 shares of common stock, a Series B Warrant to purchase 31.49606 shares of common stock and a Series C Warrant to purchase 23.622045 shares of common stock. The Notes and Warrants are immediately separable after the sale. Neither the Notes nor the Warrants are listed on a national exchange or included in any automated quotation system.

Our common stock is traded on the NASDAQ Global Market under the symbol **NGEN**. On August 24, 2007, the last reported sale price of our common stock on the NASDAQ Global Market was \$1.13 per share.

Investing in our securities involves a high degree of risk. See Risk factors beginning on page S-9 of this prospectus supplement.

Seven Hills Partners LLC has agreed to act as agent for us in connection with the arrangement of this transaction on a best efforts basis. We have agreed to pay Seven Hills Partners LLC the aggregate placement agent fee set forth in the table below. See **Plan of Distribution** beginning on page S-45 of this prospectus supplement for more information regarding this arrangement.

	Per Note	Total
Offering price	100%	\$ 20,000,000
Placement agent fees	4.8%	\$ 960,000
Proceeds, before expenses, to Nanogen, Inc.	95.2%	\$ 19,040,000

The placement agent is not purchasing or selling any of the Notes or Warrants pursuant to this prospectus supplement or the accompanying prospectus. We may determine to sell less than the maximum amount of Notes and Warrants offered pursuant to this prospectus supplement and

the accompanying prospectus. We expect that delivery of the Notes and Warrants being offered pursuant to this prospectus supplement will be made to purchasers on or about August 27, 2007. Funds from purchasers will be deposited into an escrow account and held until jointly released by us and the placement agent on the date the Notes and Warrants are to be delivered to the purchasers. All such funds received will be held in a non-interest bearing account.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus supplement or the accompanying prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

SEVEN HILLS PARTNERS LLC

The date of this prospectus supplement is August 24, 2007.

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FORWARD-LOOKING STATEMENTS

This prospectus supplement, the accompanying prospectus, and the documents incorporated herein and therein by reference include forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (or the Securities Act), and Section 21E of the Securities Exchange Act of 1934, as amended (or the Exchange Act). All statements other than statements of historical fact are forward-looking statements for purposes of these provisions, including any projections of earnings, revenues or other financial items, any statements of the plans and objectives of management for future operations, any statements concerning proposed new products or services, any statements regarding future economic conditions or performance, any statements relating to future regulatory action, and any statement of assumptions underlying any of the foregoing. In some cases, forward-looking statements can be identified by the use of terminology such as may, should, could, would, will, believes, intends, expects, plans, anticipates, estimates, potential, or continue or the n comparable terminology. Although we believe that the expectations reflected in the forward-looking statements contained in this prospectus supplement and the accompanying prospectus and in the incorporated documents are reasonable, we cannot assure you that such expectations or any of the forward-looking statements will prove to be correct, and actual results could differ materially from those projected or assumed in the forward-looking statements. Our future financial condition and results of operations, as well as any forward-looking statements, are subject to inherent risks and uncertainties, including but not limited to those set forth herein under the heading Risk Factors and those discussed in documents we incorporate by reference into this prospectus supplement and the accompanying prospectus and for the reasons described elsewhere in this prospectus supplement and the accompanying prospectus.

We will not update these forward-looking statements, whether as a result of new information, future events or otherwise. You should, however, review additional disclosures we make in our quarterly reports on Form 10-Q, current reports on Form 8-K and annual reports on Form 10-K filed with the SEC.

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A BOUT THIS PROSPECTUS SUPPLEMENT

This prospectus supplement and the accompanying prospectus dated August 2, 2007 are part of a registration statement on Form S-3 (File No. 333-144880) we filed with the Securities and Exchange Commission, or the SEC, using a shelf registration process. Under this shelf registration process, we may from time to time sell any combination of securities described in the accompanying prospectus in one or more offerings up to a total of \$50,000,000. Immediately prior to the offering, we also filed a related registration statement on Form S-3 pursuant to Rule 462(b) under the Securities Act to increase the total amount available under the shelf to \$60,000,000.

These documents contain important information you should consider when making your investment decision. The accompanying prospectus provides you with a general description of the securities we may offer. This prospectus supplement contains information about the securities issued in this offering. This prospectus supplement may add, update or change information in the accompanying prospectus. You should rely only on the information provided in this prospectus supplement, the accompanying prospectus or incorporated by reference in this prospectus supplement or the accompanying prospectus. We have not authorized anyone to provide you with any other information.

This prospectus supplement does not constitute an offer to sell or a solicitation of an offer to buy the securities offered hereby in any jurisdiction where, or to any person to whom, it is unlawful to make such offer or solicitation.

The information contained in the prospectus and the prospectus supplement is accurate only as of the date of the prospectus and the prospectus supplement, regardless of the time of delivery of this prospectus supplement or of any sale of the securities.

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SUMMARY

This summary highlights information contained elsewhere or incorporated by reference in this prospectus supplement and the accompanying prospectus. This summary does not contain all of the information that you should consider before deciding to invest in the securities. You should read this entire prospectus supplement and the accompanying prospectus carefully, including the Risk Factors section contained on page S-9 of this prospectus supplement and the Risk Factors section on page 2 of the accompanying prospectus, and our consolidated financial statements and the related notes and the other documents incorporated by reference in this prospectus supplement and the accompanying prospectus.

Our company is based on the vision of providing a higher quality of healthcare through advanced diagnostic products. Our business strategy is to assemble the companies, products and knowledge base to become a leading supplier of the technologies and products that will help drive a new era of personalized medicine. We were early to recognize that the adoption of personalized medicine is dependent on the advancement of diagnostic technologies. We believe that the commercialization of our products and technologies will help bridge the gap between early-stage scientific research and actual clinical practice. We are developing several product lines that are directly targeting specific markets within the advanced diagnostics field that have significant potential for revenue growth. We see recent successes and a growing capability in the clinical laboratories' ability to perform accurate advanced diagnostic testing as a strong validation of our strategy. In addition, the Federal Drug Administration has recently released guidance encouraging the generation of more pharmacogenomics data and molecular diagnostic testing during drug development and clinical trials, and before the use of medications. We believe these applications of advanced diagnostics will help build demand for our products and technologies.

We were incorporated under the laws of the State of Delaware and our stock is listed on the Nasdaq Global Market under the symbol **NGEN**. Our corporate offices are located at 10398 Pacific Center Court, San Diego, California 92121. Our main telephone number is 858-410-4600.

For further information regarding us and our financial information, you should refer to our recent filings with the SEC. See **Where You Can Find More Information** and **Incorporation of Certain Documents by Reference** in this prospectus supplement.

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THE OFFERING

Issuer	Nanogen, Inc.
Securities Offered	We are offering up to \$20,000,000 in aggregate principal amount of our 6.25% senior convertible notes due 2010 (the "Notes") convertible initially into an aggregate of 15,748,030 shares of our common stock, and Series A Warrants, Series B Warrants and Series C Warrants to purchase shares of our common stock, exercisable initially into an aggregate of 11,023,621 shares of our common stock, and may become exercisable for an additional 6,299,212 shares of our common stock. The Warrants represent 110% of the shares of common stock issuable upon conversion of the Notes based on the initial conversion price of \$1.27. In addition, we are offering shares of common stock issuable to the holder of a Note or Warrant upon conversion of the Note or exercise of the Warrant, and shares of common stock that may be issued in payment of interest on the Notes.
Purchase Price	For each \$100 of Notes purchased by an investor, the investor also will receive a Series A Warrant to purchase 31.49606 shares of common stock, a Series B Warrant to purchase 31.49606 shares of common stock and a Series C Warrant to purchase 23.622045 shares of common stock. The Notes and Warrants are immediately separable after the sale.
Use of Proceeds	We intend to use the net proceeds from this offering for working capital, acquisitions and other general corporate purposes, including the development and support of our sales and marketing organization, support for our continuing research and development efforts and, if opportunities arise, to acquire businesses, products, technologies or licenses that are complementary to our business and make strategic investments in businesses complementary to our business. See "Use of Proceeds" on page S-14.
Outstanding Shares of Common Stock	The number of shares of our common stock outstanding immediately prior to this offering is 73,050,915. Assuming conversion of all of the Notes sold in this offering at the initial conversion price of \$1.27, and exercise of all of the Warrants sold in this offering, the total number of shares of our common stock to be outstanding will be 106,121,778.
Risk Factors	An investment in the Notes and Warrants involves a high degree of risk. See "Risk Factors" beginning on page S-9 of this prospectus supplement and page 2 of the accompanying prospectus for a discussion of certain factors that you should consider when evaluating an investment in the Notes, Warrants and the underlying common stock.

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Summary of the Notes

(See the section entitled "Description of Notes" on page S-15 of this prospectus supplement)

Notes Offered	\$20.0 million in aggregate principal amount of unsecured senior convertible notes.
Maturity Date	Third anniversary of date of issuance, subject to extension under certain circumstances, including extension for an additional two-year period with respect to any amounts not converted as of the initial maturity date due to limitations on beneficial ownership.
Interest	Interest accrues on the Notes at an annual rate of 6.25% payable quarterly, in arrears, commencing on September 30, 2007. The interest may be paid, subject to certain conditions, in cash or shares of our common stock, or a combination of cash and shares of common stock. Upon and during the occurrence of an event of default, the interest rate under the Notes will increase to 12% per annum.
Conversion Price and Adjustment	<p>The principal amount of the Notes, together with any accrued and unpaid interest and any late charges and an interest make-whole, is convertible by the holders of the Notes, at any time following their issuance, into shares of our common stock at an initial conversion price of \$1.27 per share, subject to certain limitations on beneficial ownership.</p> <p>The conversion price is subject to certain adjustments set forth in the Indenture governing the Notes, including, without limitation, full ratchet anti-dilution protection for any equity or convertible securities issuances within 18 months of the issuance of the Notes and weighted-average anti-dilution protection thereafter, subject to customary exceptions and a limitation on the reduction of the conversion price below a \$1.2675 floor price without subsequent stockholder approval.</p>
Letter of Credit	<p>We have agreed to obtain a letter of credit from Wells Fargo Bank in the amount of \$7.0 million for the benefit of the holders. The letter of credit will permit the agent for the holders of the Notes to draw the letter of credit if an event of default exists or at maturity. The proceeds drawn under the letter of credit will be applied to reduce our payment obligations under the Notes.</p> <p>The letter of credit will be terminated if we meet certain conditions, which include, but are not limited to, all of the following: (i) the closing sales price of our common stock on the NASDAQ Global Market equals or exceeds \$1.524 per share for 20 out of 30 consecutive trading days; (ii) there is no event of default under the indenture governing the Notes; (iii) our common stock has not been suspended for trading on NASDAQ; and (iv) we have been in compliance with other transaction documents for this offering.</p>

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At closing, we will deposit \$7.3 million of the total \$20.0 million proceeds from the offering in a cash collateral account with Wells Fargo Bank to secure the letter of credit. The funds in the cash collateral account will be released to us upon the termination of the letter of credit. The Notes are not secured by any of our assets or assets of our subsidiaries, except that we have agreed to obtain the letter of credit for the benefit of the purchasers.

Mandatory Conversion

If, at any time after the 24-month anniversary of the issuance date of the Notes, the last closing sale price of our common stock on the NASDAQ Global Market exceeds \$2.2225 per share for any 20 out of 30 consecutive trading days, then we will have the right, subject to compliance with certain conditions, which include, but are not limited to, our continued listing on an eligible trading market, compliance with certain covenants and the lack of occurrence of an event of default, to require the holders of the Notes to convert all or any portion of the conversion amount of the Notes into shares of common stock at the then-applicable conversion price, subject to certain limitations on beneficial ownership.

Events of Default

The Notes will contain customary event of default provisions, including without limitation, failure to pay principal or interest when due, suspension from trading, failure to cure conversion failures or maintain sufficient shares of common stock available for conversion, breaches of covenants, breaches of material representations, failure to repay certain indebtedness exceeding \$250,000, the occurrence of bankruptcy or similar events, defaults under our agreements, and the rendering of a final judgment in excess of \$500,000 not covered by insurance.

After the occurrence of an event of default, any holder may require us to redeem all or a portion of such holder's Note at a redemption price in cash equal to the greater of (i) the product of (x) the conversion amount of the Notes to be redeemed and (y) the applicable redemption premium (120%), and (ii) the product of (A) the applicable conversion amount of the Notes to be redeemed divided by the conversion price in effect at such time as the holder delivers the redemption notice and (B) the greater of (1) closing sale price of the common stock on the date immediately preceding the event of default, and (2) the closing sale price of the common stock on the date immediately after the event of default and (3) the closing sale price of the common stock on the date the holder delivers the redemption notice.

Change of Control

In connection with a change of control transaction, the holders of the Notes will have the right to require us to redeem all of their Notes at a redemption price in cash equal to the sum of (1) unpaid interest and late charges and (2) the greater of (i) the product of (x) the conversion amount (not including interest and late charges) of the Notes being redeemed and (y) the quotient determined by dividing (A) the greater

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of the closing sale price of the common stock immediately prior to the consummation of the change of control, the closing sale price of the common stock immediately following the public announcement of such proposed change of control and the closing sale price of the common stock immediately prior to the public announcement of such proposed change of control by (B) the then applicable conversion price, and (ii) 120% of the conversion amount (not including interest and late charges) of the Notes being redeemed.

In the event of a change of control, we have the right to redeem all of the Notes at a price in cash equal to the sum of (1) unpaid interest and late charges and (2) the greater of (i) the product of (x) the conversion amount (not including interest and late charges) of the Notes being redeemed and (y) the quotient determined by dividing (A) the greater of the closing sale price of the common stock immediately prior to the consummation of the change of control, the closing sale price of the common stock immediately following the public announcement of such proposed change of control and the closing sale price of the common stock immediately prior to the public announcement of such proposed change of control by (B) the then applicable conversion price, and (ii) 120% (if the acquirer is not a publicly traded company) or 140% (if the acquirer is a publicly traded company) of the conversion amount (not including interest and late charges) of the Notes being redeemed.

Fundamental Transactions

For fundamental transactions generally, subject to the foregoing change of control provisions, we will be required to reaffirm to the holders of Notes our obligations under the Notes and other transaction documents for the offering as well as to provide a confirmation that following the consummation of the fundamental transaction, the Notes will be convertible into either (i) our common stock or other shares of publicly traded common stock (or their equivalent) of the Company, or the Company as a successor entity, or (ii) if we are not a publicly traded entity following the fundamental transaction, the securities or other cash or assets that holders of the Notes would have received had they converted the Notes immediately prior to the consummation of the fundamental transaction.

Covenants

The Notes will contain covenants which, among other things, restrict our ability to (i) incur additional indebtedness other than in connection with existing indebtedness or certain other permitted indebtedness under the terms of the Indenture, (ii) grant liens on our assets other than certain ordinary permitted liens; or (iii) make distributions on or repurchase shares of our common stock.

Late Charges

If any payment of principal, interest or other amounts payable under the Notes or other transaction documents in the offering are not paid when due, such past due amount are subject to a late charge of 15% per annum from the date due until paid.

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Summary of Warrants

(See the section entitled "Description of the Warrants" on page S-29 of this prospectus supplement)

Warrants Offered

Series A Warrants, Series B Warrants and Series C Warrants to purchase initially an aggregate of 17,322,833 share of our common stock. All Warrants are exercisable into shares of our common stock, subject to certain limitations on beneficial ownership. Series B Warrants are exercisable only if certain conditions relating to Series A Warrants are satisfied, as described below.

Exercise Amount and Price

The initial exercise price of Series A Warrants is \$1.14.

If any of the Series A Warrants are exercised, whether at the option of the holders or following the exercise of our rights to require holders to exercise, then Series B Warrants will become exercisable. The number of exercisable Series B Warrants will equal the number of Series A Warrants exercised. With respect to Series B Warrants that become exercisable in any calendar quarter, the exercise price will be equal to 110% of the closing sales price of our common stock on the last trading day of such calendar quarter. On the date when all of Series A Warrants are exercised, the exercise price for any previously unexercised Series B Warrants will be equal to 110% of the closing sales price of our common stock on such date. The exercise price of the Series B Warrants is subject to a floor, so that its exercise price cannot be less than \$1.13 per share without stockholder approval.

The initial exercise price of Series C Warrants is \$1.14.

Expiration Dates

Series A Warrants and Series C Warrants are exercisable at any time from the date of issuance until the fifth (5th) anniversary of the date of issuance. Series B Warrants are exercisable from the date on which they become exercisable until the third (3rd) anniversary of such date.

Mandatory Exercise Rights

At any time following the termination of the letter of credit, if the closing sales price of our common stock is at least 135% of the applicable exercise price of Series A Warrants for 20 out of 30 consecutive trading days, we may, subject to certain conditions, require the holders to exercise the Series A Warrants.

After six months following the issuance date of the Warrants, and at least thirty (30) trading days following (i) the exercise of all of the Series A Warrants and (ii) termination of the letter of credit, if the closing sales price of our common stock is at least 125% of the exercise price of Series C Warrants for 20 out of 30 consecutive trading days, we may, subject to certain conditions, require the holders to exercise the Series C Warrants.

Exercise Price Adjustment

The exercise price of the Warrants is subject to certain adjustments set forth in the Warrants, including, without limitation, full ratchet

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anti-dilution protection for any equity or convertible securities issuances within eighteen (18) months of the issuance of the Warrants and weighted-average anti-dilution protection thereafter, subject to customary exceptions and a limitation on the reduction of the exercise price below \$1.13 without stockholder approval.

Fundamental Transaction

In the event of a fundamental transaction (as defined in the Warrants), the Warrant holder may require us to purchase the Warrant for cash at a price equal to the value of the remaining unexercised portion of the Warrant determined using the Black-Scholes Option Pricing Model. For fundamental transactions generally, subject to the foregoing provision, we will be required to reaffirm to the holders our obligations under the financing agreements as well as to provide a confirmation that following the consummation of the fundamental transaction, the Warrant will be exercisable into either (i) our common stock or other shares of publicly traded common stock (or their equivalent) of the Company, or the Company as the successor entity, or (ii) if we are not a publicly traded entity following the fundamental transaction, the securities or other cash or assets that the holder of the Warrant would have received had it exercised the Warrant immediately prior to the consummation of the fundamental transaction.

Cashless Exercise; Payments for Failure to Deliver Shares

The Warrants may only be exercised on a cashless exercise basis if the registration statement covering the issuance of shares upon exercise of the Warrants is not available at the time of exercise of such Warrants. The Warrants contain provisions requiring us to make cash payments to a Warrant holder in amounts described in the Warrants for failure to timely deliver shares of common stock upon exercise all or a portion of the Warrant by a holder.

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RISK FACTORS

An investment in our securities offered through this prospectus supplement and the accompanying prospectus involves certain risks. You should carefully consider the specific risks relating to this offering, the Notes and the Warrants set forth below and relating to our business set forth under the caption "Risk Factors" in our filings with the Securities and Exchange Commission pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Securities Exchange Act of 1934, as amended, incorporated by reference herein, before making an investment decision. The risks and uncertainties we have described are not the only ones facing our company. Additional risks and uncertainties not presently known to us or that we currently consider immaterial may also affect our business operations.

Risks Related to this Offering and the Notes and Warrants

Management will have broad discretion as to the use of the proceeds from this offering, and we may not use the proceeds effectively.

We have not designated the amount of net proceeds we will use for any particular purpose. Accordingly, our management will have broad discretion as to the application of the net proceeds and could use them for purposes other than those contemplated at the time of this offering. Our stockholders may not agree with the manner in which our management chooses to allocate and spend the net proceeds. Moreover, our management may use the net proceeds for corporate purposes that may not increase our profitability or our market value. See "Use of Proceeds" at page S-14 for a description of our management's intended use of the proceeds from this offering.

Our substantial indebtedness after the completion of the offering could adversely affect our financial condition and our ability to respond to changes in our business.

We will be highly leveraged and have significant debt service obligations following the completion of this offering. The increased debt obligations could have significant negative consequences, including, but not limited to:

increasing our vulnerability to general adverse economic and industry conditions;

limiting our ability to obtain additional financing in the future for working capital, capital expenditures, acquisitions or other business purposes;

limiting our flexibility to plan for, or react to, changes in our business and the industry in which we compete;

placing us at a possible competitive disadvantage to competitors with fewer debt obligations and competitors that have better access to capital resources; and

requiring us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness, thereby reducing the availability of our cash flow to fund working capital expenditures, research and development efforts and other general corporate purposes.

The Notes provide that upon the occurrence of various events of default and change of control transactions, the holders would be entitled to require us to redeem the Notes for cash. We may not have the funds necessary to redeem the Notes for cash, or any such redemption of the Notes could leave us with little or no working capital for operations or capital expenditures.

The Notes allow each holder to require us to redeem the Notes upon the occurrence of various events of default, such as the termination of trading of our common stock on a qualified stock market or a breach by us of the covenants set forth in the Indenture and in other agreements, such as covenants that restrict our ability to incur additional indebtedness, grant liens on our assets or make distributions on or repurchase shares of our common stock. The Notes will also allow each holder to require us to redeem the Notes upon specified change of control transactions. In such a situation, we may be required to redeem all or part of the Notes, including any

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accrued interest, redemption premium and penalties. Some of the events of default include matters over which we may have little or no control. If an event of default or a change of control occurs, we may be unable to repay the full price in cash. Even if we were able to prepay the full amount in cash, any such repayment could leave us with little or no working capital for our business. We have not established a sinking fund for payment of our obligations under our Notes, nor do we anticipate doing so. In addition, upon the occurrence of an event of default, the holders may draw under the letter of credit, in which case we will lose access to the funds in the cash collateral account, which will have an adverse effect on our ability to meet our cash needs and payment obligations.

We may not have sufficient funds to make required payments on the Notes.

Our liquidity position is constrained by the operating losses from our business, and we expect to incur net operating losses for the foreseeable future. As a result, we may not have sufficient funds to make the interest (if we are required to pay interest in cash) and principal payments on the Notes when due, either at maturity or upon the occurrence of various events of default or specified change of control transactions. Neither the Indenture nor the terms of the Notes require us to achieve or maintain any minimum financial ratios relating to our financial position or results of operations. If we do not have sufficient funds to make these payments, we will have to obtain an alternative source of funds, including sales of our assets or assets of our subsidiaries, sales of our equity securities or capital or debt securities. We cannot assure you that we will be able to obtain sufficient funds to meet our payment obligations under the Notes through any of these alternatives. Failure to do so will have a material adverse effect on our business, financial position and results of operations.

If we are not able to access the funds in the cash collateral account, it will adversely affect our cash flow, financial results and our ability to meet payment obligations.

We have agreed to initially deposit \$7.3 million of the total \$20 million purchase price of the Notes in a cash collateral account for the purpose of securing the letter of credit issued in favor of the holders of the Notes. The funds in the cash collateral account, including interests earned, will be released to us only if we meet certain conditions to terminate the letter of credit. These conditions include, but are not limited to, all of the following: (i) the closing sales price of our common stock on the NASDAQ Global Market equal to or exceeds \$1.524 per share for 20 out of 30 consecutive trading days; (ii) there is no event of default under the Indenture; and (iii) our common stock has not been suspended from trading on NASDAQ Global Market. There is no guarantee that we will meet all of the conditions for the termination of the letter of credit. In addition, there is no guarantee that the price of our common stock will reach the target level described above, and even if it does, there is no assurance that the price will maintain at such level for the required period of time. If the price of our common stock does not meet this requirement or if we cannot meet any of the conditions, we will not have access to the funds in the cash collateral account, which will adversely affect our cash flow, financial results and our ability to meet payment obligations under the Notes.

We may not be able to refinance the Notes if required or if we so desire.

We may need or desire to refinance all or a portion of the Notes or any other future indebtedness that we incur on or before the maturity of the Notes. There can be no assurance that we will be able to refinance any of our indebtedness on commercially reasonable terms, if at all. If we are unable to generate sufficient cash flow or refinance our debt on favorable terms, it could adversely affect our financial condition.

There are certain conversion and exercise restrictions associated with the Notes and the Warrants.

The Notes and the Warrants may not be converted or exercised if the holder of the respective security (together with its affiliates) would beneficially own in excess of 4.99% of our outstanding common stock following such exercise or conversion. By written notice to us, the holders may increase this percentage not in excess of 9.99%.

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The Notes and Warrants are new issue of securities, and there is no existing market for the Notes and the Warrants.

We do not intend to apply for listing of the Notes or the Warrants on any securities exchange or for quotation of the Notes on any automated dealer quotation system. A market may not develop for the Notes or the Warrants, and if a market does develop, it may not be sufficiently liquid for your purposes. If an active, liquid market does not develop for the Notes and Warrants, the market price and liquidity of the Notes and Warrants may be adversely affected. If any of the Notes and Warrants are traded after their initial issuance, they may trade at a discount from their initial offering price.

The liquidity of the trading market, if any, and future trading prices of the Notes and Warrants will depend on many factors, including, among other things, the market price of our common stock, prevailing interest rates, our operating results, financial performance and prospects, the market for similar securities and the overall securities market, and may be adversely affected by unfavorable changes in these factors. Historically, the market for convertible debt has been subject to disruptions that have caused volatility in prices. The market for the Notes and Warrants may be subject to disruptions that could have a negative effect on the holders of the Notes, regardless of our operating results, financial performance or prospects.

The right of holders of Notes to receive payments on the Notes is effectively subordinated to all existing and future liabilities of our subsidiaries and to all of our existing and future secured debt.

None of our subsidiaries will guarantee our obligations under, or have any obligation to pay any amounts due on, the Notes. As a result, the Notes will be effectively subordinated to all liabilities of our subsidiaries. Our rights and the rights of our creditors, including holders of the Notes, to participate in the distribution of the assets of any of our subsidiaries upon their liquidation or recapitalization will generally be subject to the prior claims of those subsidiaries' creditors. In addition, the Notes will not be secured by any of our assets or those of our subsidiaries, except that we have agreed to obtain the letter of credit for the benefit of the purchasers. As a result, the Notes will be effectively subordinated to any secured debt we may incur. In any liquidation, dissolution, bankruptcy or other similar proceeding, holders of our secured debt may assert rights against any assets securing such debt in order to receive full payment of their debt before those assets may be used to pay the holders of the Notes. In such an event, we may not have sufficient assets remaining to pay amounts due on any or all of the Notes.

Conversion of the Notes and exercise of Warrants and issuance of shares of common stock in payment of interests on the Notes will dilute the ownership interest of existing stockholders, including holders who had previously converted their Notes.

The conversion or exercise of some or all of the Notes and Warrants, respectively, and the issuance of shares of common stock in payment of interests on the Notes, could significantly dilute the ownership interests of existing stockholders. Any sales in the public market of the common stock issuable upon such conversion or exercise could adversely affect prevailing market prices of our common stock. In addition, the existence of the Notes may encourage short selling by market participants because the conversion of the Notes could be used to satisfy short positions, or anticipated conversion of the Notes into shares of our common stock could depress the price of our common stock.

We have agreed to certain limitations on our ability to sell our securities in future financings, which may restrict our ability to raise capital.

We have agreed, for so long as any Notes or Warrants remain outstanding, that we will not issue or sell, subject to certain exceptions, shares of our common stock for a consideration per share less than the conversion price of the Notes or the exercise price of the Warrants immediately prior to such sale, if the effect of the issuance or sale is to cause the conversion price or exercise price to be adjusted below the fixed floor prices set forth in the Indenture or the Warrant, or otherwise cause us to breach our obligations under applicable rules of NASDAQ. In addition, we have agreed, for so long as any Notes or Warrants remain outstanding, that we will

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not to sell subject to certain exceptions, securities with a conversion or exercise price that varies from the market price of our common stock. These limitations will restrict our ability to raise capital through equity financing in the future. If we cannot raise more capital or obtain additional financings on terms satisfactory to us, we will have to reduce our capital expenditures, scale back our development of new products, significantly reduce our workforce and seek to license to others products or technologies that we otherwise would seek to commercialize ourselves, which will have an adverse effect on our business operations and financial results.

Restrictive covenants in the Indenture governing the Notes may limit our ability to expand our operations and capitalize on our business opportunities.

The Indenture governing the Notes includes covenants which limit our ability to borrow money, create liens, and engage in certain other activities. These restrictive covenants may limit our ability to expand our operations and capitalize on business opportunities. If we are unable to expand our operation or otherwise capitalize on our business opportunities, our business, financial condition and results of operations could be materially adversely affected and we may not be able to meet our debt service obligations.

The Notes will likely be subject to the contingent payment debt instrument rules, and holders will likely be required to include amounts in income in excess of the stated interest payable on the Notes and may recognize ordinary income on a conversion of a Note. Gain recognized with respect to a Note will generally be treated as ordinary interest income.

We intend to take the position that the Notes will be subject to the contingent payment debt instrument rules. The application of those rules to instruments such as the Notes is uncertain, however, and no assurance can be given that the Internal Revenue Service, or IRS, will agree with the positions we intend to take. We have not sought or received an IRS ruling or an opinion of counsel regarding the application of the contingent payment debt instrument rules to the Notes. Each holder of a Note should consult its own tax advisor concerning the tax consequences of ownership and disposition of the Notes.

Under the contingent payment debt instrument rules, (i) each holder generally will be required to accrue interest on the Notes based on the yield of a comparable nonconvertible, noncontingent fixed-rate debt instrument with terms and conditions otherwise similar to the Notes (subject to certain adjustments to such accruals of income), with the result that a holder is likely to recognize taxable income in excess of the regular interest payments received while the Notes are outstanding, (ii) the amount realized by a holder upon the conversion of a Note (including the fair market value of common stock received upon conversion) would generally be treated as a contingent payment under the contingent payment debt instrument rules, which could result in the recognition of ordinary interest income on a conversion and (iii) any gain recognized on a sale, exchange, redemption or retirement of a Note generally would be treated as ordinary interest income (subject to potential adjustments) and any loss would generally be ordinary loss to the extent of interest previously included in income and, thereafter, capital loss.

We may need additional capital in the future. If additional capital is not available, we may have to curtail or cease operations.

The proceeds we will receive in the offering will not be sufficient to complete the research and development necessary to bring our products to market and to further our manufacturing and marketing capabilities. We may need to raise additional funds, and we may seek such funds through public and private securities offerings, arrangements with corporate partners, borrowings under lease lines of credit or other sources. If we cannot raise more money, we will have to reduce our capital expenditures, scale back our development of new products, significantly reduce our workforce and seek to license to others products or technologies that we otherwise would seek to commercialize ourselves. The amount of money we will need will depend on many factors, including among others:

the amount of revenue we are able to generate;

the progress of our research and development programs;

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the commercial arrangements we may establish;

the time and costs involved in:

scaling up our manufacturing capabilities;

meeting regulatory requirements, including meeting necessary Quality System Regulations (QSRs) and obtaining necessary domestic and international regulatory clearances or approvals;

acquisition(s) or investment(s) into other businesses;

filing, prosecuting, defending and enforcing patent claims and litigation; and

the scope and results of our future clinical trials, if any.

Additional capital may not be available on terms acceptable to us, or at all. Any additional equity financing will be dilutive to stockholders, and debt financing, if available, may include restrictive covenants and require significant collateral.

We could lose our listing on the NASDAQ Global Market if our stock price falls below \$1.00 for 30 consecutive days, and the loss of the listing would make our stock significantly less liquid and would affect its value.

The Notes and Warrants are convertible into or exercisable for our shares of common stock. Our common stock is listed on the NASDAQ Global Market and NASDAQ's marketplace rules for continued listing on the NASDAQ Global Market require, among other things, that the bid price for our common stock not fall below \$1.00 per share for a period of 30 consecutive trading days. The closing bid price for our common stock on August 24, 2007 was \$1.13 per share. If, in the future, our minimum bid price is below \$1.00 for 30 consecutive trading days, under the current NASDAQ Global Market rules we will have a period of 180 days to attain compliance by meeting the minimum bid price requirement for 10 consecutive days during the compliance period. If our common stock fails to maintain a minimum bid price of \$1.00 for 30 consecutive days during a 180-day grace period on the NASDAQ Global Market, we could receive a delisting notice from the NASDAQ Global Market. Upon delisting from the NASDAQ Global Market, our stock would be traded over-the-counter, more commonly known as OTC. OTC transactions involve risks in addition to those associated with transactions in securities traded on the NASDAQ Global Market. Many OTC stocks trade less frequently and in smaller volumes than NASDAQ-listed stocks. Accordingly, our common stock would be less liquid than it would otherwise be. Also, the values of these stocks may be more volatile than NASDAQ-listed Stocks. In addition, our common stock could then potentially be subject to the SEC's penny stock rules, which place additional disclosure requirements on broker-dealers. These additional disclosure requirements may harm your ability to sell shares if it causes a decline in the ability or willingness of broker-dealers to sell our common stock. If our stock is traded in the OTC market and a market maker sponsors us, we may have the price of our stock electronically displayed on the OTC Bulletin Board, or OTCBB. However, if we lack sufficient market maker support for display on the OTCBB, we must have our price published by the National Quotations Bureau LLP in a paper publication known as the Pink Sheets. The marketability of our stock would be even more limited if our price must be published on the Pink Sheets.

Table of Contents**RATIO OF EARNINGS TO FIXED CHARGES**

The following table sets forth our ratio of earnings to fixed charges, and our coverage deficiency. We calculated the ratio of earnings to fixed charges by dividing earnings by total fixed charges. Earnings are defined as income (loss) before provision for income taxes and minority interest plus fixed charges less minority interest in pre-tax income of subsidiaries that have not incurred fixed charges. Fixed charges are defined as the sum of interest expensed plus amortized capitalized expenses related to indebtedness plus an estimate of the interest within rental expense. We do not currently have, and during the periods prescribed did not have, any preferred stock outstanding.

(in thousands, unaudited)	For Year Ended December 31,					For Six Months Ended
	2002	2003	2004	2005	2006	June 30, 2007
Ratio of Earnings to Fixed Charges(1)						
Deficiency of earnings available to cover fixed charges	\$ (24,402)	\$ (32,413)	\$ (38,907)	\$ (96,494)	\$ (49,070)	\$ (26,379)

(1) For all periods presented, earnings were insufficient to cover fixed charges

USE OF PROCEEDS

We estimate that the net proceeds we will receive from this offering, excluding the proceeds, if any, from the exercise of the Warrants issued in this offering, will be approximately \$19.04 million, after deducting the placement agent fees and estimated offering expenses. We would also receive additional funds in the event of any cash exercise of the Warrants. We are required at closing to deposit \$7.3 million in cash from the proceeds of the offering in a cash collateral account with Wells Fargo Bank to secure our reimbursement obligations in respect of the letter of credit. For more information about the letter of credit and the cash collateral account, see the section below entitled *Letter of Credit* under the heading *Description of Notes*.

We intend to use the net proceeds we receive from sales of the securities offered hereby for working capital, acquisitions and other general corporate purposes, including the development and support of our sales and marketing organization, support for our continuing research and development efforts and, if opportunities arise, to acquire businesses, products, technologies or licenses that are complementary to our business and make strategic investments in businesses complementary to our business. We periodically review acquisition and strategic investment opportunities that are related to our business and we believe that it is desirable to have funds on hand so as to be able to make acquisitions and strategic investments promptly. As of the date of this prospectus supplement, we have no specific agreements, understandings, commitments or arrangements with regard to any particular future acquisition or strategic investment, and no assurance can be given that we will be able to consummate any such acquisitions or strategic investments or that, if consummated, such acquisitions or investments would be on terms that are favorable to us.

Pending these uses, we intend to invest the proceeds of this offering in short-term, investment grade interest-bearing securities.

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DESCRIPTION OF NOTES

We will issue the Notes under an indenture to be dated on or about August 27, 2007 (the "base indenture") and a first supplemental indenture to be dated on or about August 27, 2007 (the "first supplemental indenture" and, together with the base indenture, the "Indenture") between us and The Bank of New York Trust Company, N.A. as trustee (the "Trustee"). We have summarized the material provisions of the Indenture below. The following description is not complete and is subject to, and qualified by reference to, all of the provisions of the Indenture and the Notes, which we urge you to read because they, and not this Description of Notes, define your rights as a Note holder. A copy of the Indenture and the Form of the Notes will be included as exhibits to a Current Report on Form 8-K that we will file with the SEC and that will be incorporated by reference into the registration statement of which this prospectus supplement forms a part. You may also request a copy of the Indenture and the Form of the Notes from us as described under "Where You Can Find More Information."

General

The Notes:

are in an aggregate principal amount of \$20 million;

are convertible, at the holder's option, into shares of our common stock at an initial conversion price of \$1.27 per share;

are redeemable, at the holder's option, upon the occurrence of an event of default or change of control transaction;

may be redeemed by us upon the occurrence of a change of control transaction;

bear interest at an annual rate of 6.25%, payable quarterly on the last day of March, June, September and December of each year (each, an "Interest Date"), with the first Interest Date being September 30, 2007;

are due and payable on August 27, 2010, unless earlier converted or redeemed, subject to extension for an additional two-year period with respect to amounts not converted as of the initial maturity date due to limitations on beneficial ownership;

are unsecured; and

are supported by a letter of credit.

Interest

Interest on the outstanding principal amount of the Notes shall be payable quarterly in arrears on each Interest Date. Interest shall accrue at 6.25% per annum from the most recent date to which interest has been paid, or if no interest has been paid, from August 24, 2007, until the principal amount of the Notes is paid. From and after the occurrence and during the continuance of an Event of Default (as defined in the section entitled "Redemption" below), the interest rate shall be increased to 12.0%. If such Event of Default is subsequently cured, the increased interest rate will cease to be effective as of the date of such cure; provided that the interest calculated at the increased rate during the continuance of such Event of Default will continue to apply. In addition, if any payment of principal or other amounts payable under the Notes or other transaction documents in the offering are not paid when due, such past due amount are subject to a late charge of 15% per annum from the date due until paid.

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Interest under the Notes will be payable on each Interest Date in shares of common stock so long as there has been no Equity Conditions Failure (as defined below in the section entitled *Conversion* below) unless the holder has waived such Equity Conditions Failure), in which case we would be required to pay the interest in cash. We may, at our option, pay interest in cash or a combination of common stock (so long as there has been no

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Equity Conditions Failure) and cash. If any interest is to be paid in common stock, then we will pay to each holder a number of shares of common stock equal to (I) the amount of interest payable on the applicable Interest Date in common stock divided by (II) the applicable interest conversion price, which shall equal the lower of (i) the applicable Conversion Price (as defined below) and (ii) the price computed as ninety percent (90%) of the average of the volume weighted average price for our common stock for the five (5) trading days ending on the trading day immediately preceding the Interest Date. However, if the resulting calculation of the interest conversion price would be less than \$1.13, then we must pay interest in cash.

We will deliver a written notice to each holder of the Notes on or prior to the tenth (10th) trading day prior to the Interest Date, and such notice will (A) either (x) confirm that interest to be paid on such Interest Date will be paid entirely in shares of common stock or (y) inform you of our election to pay interest in cash or a combination of cash and common stock and specify the amount of interest that shall be paid in cash and the amount of interest, if any, that will be paid in common stock and (B) certify that there has been no Equity Conditions Failure.

If we pay interest in shares of our common stock, we will (i) issue and deliver on the applicable Interest Date to the address set forth in the register maintained by our paying agent or to such address as specified by the holder in writing to us at least two (2) business days prior to the applicable Interest Date, an unlegended certificate, registered in the name of such holder or its designee, for the number of shares of common stock to which such holder shall be entitled and (ii) with respect to each Interest Date, pay to such holder, in cash by wire transfer of immediately available funds, the amount of any cash interest. We are not entitled to pay interest in common stock and will be required to pay all interest in cash if, unless consented to in writing by such holder, there has been an Equity Conditions Failure.

An **Equity Conditions Failure** means that on any day during the period commencing ten (10) trading days prior to the applicable date of determination (e.g., Interest Date or Mandatory Conversion Date (as defined below)) the following Equity Conditions have not been satisfied (or waived in writing by each holder).

on each day during the period beginning 60 days prior to the applicable date of determination and ending on and including the applicable date of determination (the **Equity Conditions Measuring Period**), all shares of common stock issuable upon conversion of the Notes, exercise of the Warrants and as interest shall be eligible for sale without restriction other than any restrictions on sale imposed on the holder by virtue of the holder being our affiliate;

during the Equity Conditions Measuring Period our common stock is designated for quotation on the NASDAQ Global Market or any other eligible market and shall not have been suspended from trading on such exchange or market, subject to certain exceptions, nor shall delisting or suspension by such exchange or market been threatened or pending either (A) in writing by such exchange or market or (B) by falling below the then effective minimum listing maintenance requirements of such exchange or market;

during the Equity Conditions Measuring Period, we shall have delivered shares upon conversion of the Notes and upon exercise of the Warrants to the holders on a timely basis;

any applicable shares of common stock to be issued in connection with the event requiring determination may be issued in full without violating the terms of the Notes and the rules or regulations of NASDAQ; provided, however, that in the event that such shares of common stock cannot be issued in full, we shall be permitted to issue to the holder the maximum amount of shares of common stock without causing any such violation;

during the six-month period preceding the applicable date of determination, we shall not have failed to timely make any payments within five business days of when such payment is due pursuant to any transaction document executed in connection with the offering of the Notes and the Warrants;

during the Equity Conditions Measuring Period, there shall not have occurred either (i) the public announcement of a pending, proposed or intended Fundamental Transaction (as defined below) which

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has not been abandoned, terminated or consummated, or (ii) an Event of Default or (iii) an event that with the passage of time or giving of notice would constitute an Event of Default, unless cured or waived by each holder;

we shall have no knowledge of any fact that would cause any shares of common stock issuable upon conversion of the Notes or as interest and shares of common stock issuable upon exercise of the Warrants not to be eligible for sale without the need for registration under any applicable federal or state securities laws, other than any restrictions imposed on the holder by virtue of its status as our affiliate; and

we otherwise shall have been in material compliance with and shall not have materially breached any provision, covenant, representation or warranty of any transaction document executed in connection with this offering.