UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-K

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

For the Fiscal Year Ended December 31, 2020

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the Transition Period From __________to __________

Commission File Number 000-22897

NOVATION COMPANIES, INC.
(Exact Name of Registrant as Specified in its Charter)

Maryland	**74-2830661**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
9229 Ward Parkway, Suite 340, Kansas City, MO	**64114**
(Address of Principal Executive Office)	(Zip Code)

Registrant's Telephone Number, Including Area Code: (816) 237-7000

Securities Registered Pursuant to Section 12(b) of the Act:
None

Securities Registered Pursuant to Section 12(g) of the Act:
Title of Each Class
Common Stock, $0.01 par value

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

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

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, a 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 has filed a report on and attestation to its management's assessment of the effectiveness of its internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act (15 U.S.C. 7262(b)) by the registered public accounting firm that prepared or issued its audit report. ☐

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

The aggregate market value of voting and non-voting stock held by non-affiliates of the registrant as of June 30, 2020 was approximately $1,574,911, based upon the closing sales price of the registrant's common stock on that date ($.02).

Indicate by check mark whether the registrant has filed all documents and reports required to be filed by Section 12, 13 or 15(d) of the Securities Exchange Act of 1934 subsequent to the distribution of securities under a plan confirmed by a court. Yes ☒ No ☐

The number of shares of the registrant's common stock outstanding on February 25, 2021 was 116,655,893.

NOVATION COMPANIES, INC.
FORM 10-K
For the Fiscal Year ended December 31, 2020

TABLE OF CONTENTS

PART I

Unless the context otherwise requires, references in this Annual Report on Form 10-K (this "Form 10-K") to "Novation," the "Company," "NOVC," "we," "us" and "our," refer to Novation Companies, Inc. and its consolidated subsidiaries and their respective predecessors.

Forward-Looking Statements

Statements in this report regarding Novation and its business that are not historical facts are "forward-looking statements" within the meaning of Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). Forward-looking statements are those that predict or describe future events, do not relate solely to historical matters and include statements regarding management's beliefs, estimates, projections, and assumptions with respect to, among other things, our future operations, business plans and strategies, as well as industry and market conditions, all of which are subject to change at any time without notice. Words such as "believe," "expect," "anticipate," "promise," "plan," and other expressions or words of similar meanings, as well as future or conditional auxiliary verbs such as "would," "should," "could," or "may" are generally intended to identify forward-looking statements. Risks, uncertainties, contingencies, and developments, including those discussed in "Risk Factors" and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in this report could cause our future operating results to differ materially from those set forth in any forward-looking statement. Given these uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. We disclaim any obligation to update any such factors or to publicly announce the results of any revisions to any of the forward-looking statements contained herein to reflect future results, events or developments.

Item 1. Business

Overview

Novation Companies, Inc. and its subsidiaries (the "Company," "Novation," "we," "us," or "our") through Healthcare Staffing, Inc. ("HCS"), our wholly-owned subsidiary acquired on July 27, 2017, provide outsourced health care staffing and related services in the State of Georgia. Our common stock, par value $0.01 per share, is traded on OTC Pink under the symbol "NOVC".

Recent Developments

Note Refinancing and 2017 Notes. On August 9, 2019, the Company and Taberna Preferred Funding I, Ltd. ("Taberna I"), Taberna Preferred Funding II, Ltd. ("Taberna II") and Kodiak CDO I Ltd. ("Kodiak" and, together with Taberna I and Taberna II, the "Noteholders") executed a First Amendment to Senior Secured Note Purchase Agreement (the "Amendment") amending the terms of the Note Purchase Agreement (as defined below) and the 2017 Notes (as defined below) to, among other things, significantly reduce the interest rate applicable from January 2019 through the third quarter of 2028 and allow the Company to apply certain surplus interest payments against future quarterly interest payments. This amendment qualified as a troubled debt restructuring. As of December 31, 2020, the Company had $85.9 million in aggregate borrowings outstanding under three senior secured promissory notes (the "2017 Notes"). The unpaid principal amounts of the 2017 Notes bear interest at the following rates until the maturity date on March 30, 2033, with interest payable quarterly in arrears as follows: 1% per annum from April 1, 2019 through December 31, 2023; 2% per annum from January 1, 2024 through December 31, 2028; and 10% per annum from January 1, 2029 through the maturity date. Commencing with the delivery to the Noteholders of the financial statements for the fiscal year ending December 31, 2019, the Company is required to remit 50% of excess cash flow each year to the Noteholders to be applied as a principal reduction to the outstanding balance of the debt. The 2017 Notes generally rank senior in right of payment to any existing or future subordinated indebtedness of the Credit Parties (as defined below). The Company may at any time upon 30 days' notice to the Noteholders redeem all or part of the 2017 Notes at a redemption price equal to 101% of the principal amount redeemed plus any accrued and unpaid interest thereon. The 2017 Notes were entered into on July 27, 2017 as a result of a refinancing of the Company's then outstanding senior notes with the same aggregate principal amount through the execution of the Senior Secured Note Purchase Agreement, dated as of the same date (as amended, the "Note Purchase Agreement"), with Novation Holding, Inc., a wholly-owned subsidiary of the Company ("NHI") and HCS as guarantors (together with the Company, collectively, the "Credit Parties").

On April 1, 2019 and on July 1, 2019, the Company made payments under the 2017 Notes totaling $2.6 million. The actual aggregate amounts due for those dates totaled $0.4 million. Under the terms of the Amendment, the Company is permitted to apply the payment surplus of $2.2 million against future quarterly interest payments. Therefore, the Company will not have another quarterly interest payment due until April 1, 2022.

The Note Purchase Agreement contains customary affirmative and negative covenants, including but not limited to certain financial covenants. Under the terms of the Amendment, the financial covenants have been waived until the quarter ending December 31, 2021. The Note Purchase Agreement also contains customary events of default, including but not limited to payment defaults, cross defaults with certain other indebtedness, breaches of covenants and bankruptcy events. In the case of an event of default, the Noteholders may, among other remedies, accelerate the payment of all obligations under the Note Purchase Agreement and the 2017 Notes. The Credit Parties entered into a Pledge and Security Agreement, dated as of the same date, pursuant to which each of the Credit Parties granted a first priority lien generally covering all of its assets, other than accounts receivable and inventory, for the benefit of the Noteholders, to secure the obligations under the Note Purchase Agreement and the 2017 Notes.

Under the terms of the Amendment, the Company issued to the Noteholders 9,000,000 shares of common stock of the Company and ten-year warrants allowing the Noteholders to purchase up to 22,250,000 shares of the Company's common stock at an exercise price of $0.01 per share. These warrants can be exercised at any time prior to expiration. See the Company's discussion in Note 6 to the consolidated financial statements for additional information regarding the Amendment.

Business

Established in 1995, HCS is the largest outsourced healthcare services provider in the State of Georgia. HCS delivers outsourced full-time and part-time employees primarily to Community Service Boards ("CSB"). HCS has long-term relationships with many of its customers and has been providing services to several clients for more than 15 years. A CSB is a quasi-state organization providing behavioral health services at facilities across Georgia including mental health services, developmental disabilities programs and substance abuse treatments. The State of Georgia has a total of 25 CSBs. Each CSB has a number of facilities, including crisis centers, outpatient centers and 24-hour group homes that require a broad range of employees, such as registered nurses, social workers, house parents and supervisors. The CSB market in Georgia is large and growing steadily, as the demand for the services provided by the CSB continues to grow. In addition to providing outsourced employees to CSBs, HCS also provides healthcare outsourcing and staffing services to hospitals, schools, crisis units, clinics, doctors offices, prisons and a variety of privately owned businesses. The services and positions provided to these clients are similar to the ones provided to CSB clients.

Strategy

The strategy of HCS is to continue expanding its market share in providing healthcare staffing services in Georgia and in particular serving Georgia CSBs. HCS is the dominant player in providing services to Georgia CSBs and plans to increase its market share of the CSB business. HCS will also continue to expand business to additional hospitals, private group homes, clinics, rest homes, prisons and retirement centers. Furthermore, the HCS strategy includes expanding clerical staff within existing customers, as well as gaining new clients. The longer-term strategy includes expansion beyond the Georgia market and may include acquisitions of staffing companies outside of Georgia, particularly in states that have public health infrastructure similar to that of Georgia.

Competition

HCS competes with numerous national staffing and recruiting businesses that specialize in the medical and healthcare industry, such as Nursefinders, Lighthouse Recruiting, Action Med and Brightstar. Other national staffing businesses have divisions that compete with HCS in Georgia, including ATC Healthcare, Kelly Services, Interim, Randstad and Maxim. Numerous Georgia non-national and smaller staffing providers also compete with HCS.

Regulation

The healthcare industry is subject to extensive and complex federal, state and local laws and regulations related to, among other things, conduct of operations, and costs and payment for services. HCS is not directly regulated as a healthcare provider, although the customers of HCS are highly regulated. Therefore, HCS complies with many of the regulations prescribed for its customers.

HCS provides services directly to its clients on a contract basis and receives payment directly from them. However, many clients are reimbursed under the federal Medicare program and state Medicaid programs for the services they provide. Therefore, HCS also may be affected indirectly by reimbursement changes in government programs, particularly Medicare and Medicaid.

Employees

As of February 25, 2021, the Company employed 1,025 full-time employees and 388 part-time employees. None of the Company's employees are represented by a union or covered by a collective bargaining agreement.

Additional Information

The Company is a Maryland corporation formed on September 13, 1996 as "CapStar Financial, Inc." The Company's name was changed to "NovaStar Financial, Inc." effective October 11, 1996, and to "Novation Companies, Inc." effective May 23, 2012. Our corporate executive offices are located at 9229 Ward Parkway, Suite 340, Kansas City, MO 64114 and our telephone number is (816) 237-7000. Our website address is www.novationcompanies.com. Our website is not intended to be a part of, nor are we incorporating it by reference into, this Form 10-K. Our Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act are available, free of charge, on our website as soon as reasonably practicable after we electronically file this material with, or furnish it to, the SEC. Reports and other information we file with the SEC may also be viewed at the SEC's website at www.sec.gov.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the following risk factors, as well as the other information contained in this Form 10-K, including our consolidated financial statements and notes thereto, before deciding whether to invest in our common stock. Any of these risks, as well as additional risks and uncertainties that we are unaware of, could negatively affect our results of operations, financial condition, liquidity and business prospects, and cause the trading price of our common stock to decline, and cause you to lose all or part of your investment.

Risks Related to our Business and Industry

Our operations and financial results have been negatively affected by the ongoing COVID-19 pandemic and could continue to be negatively impacted, perhaps materially, by the COVID-19 pandemic.

The COVID-19 pandemic has harmed our ability to staff employees and has negatively impacted the Company's revenue. HCS relies on staffing healthcare professionals to generate income, primarily to CSBs, which are ultimately funded by the State of Georgia. The spread of COVID-19 has reduced our ability to provide these services based on customer driven lay-offs or reduction in hours of the staff provided by HCS. In addition, some CSB sponsored programs have been shut down as a result of COVID-19.

While HCS employees provide services throughout the State of Georgia at multiple facilities, the Company's operations are limited to this region. If Georgia experiences a second severe outbreak of COVID-19, it could have a larger impact on the Company and its business than on businesses which operate in multiple states.

The COVID-19 pandemic, and any other outbreak or other public health crises, may also impact our ability to attract and retain employees or healthcare professionals due to illness, risk of illness, quarantines, or other factors. Some of our healthcare professionals have been exposed, diagnosed and or quarantined as a result of COVID-19. As such, there is a risk that our employees may not want, or be able to provide services, which could negatively impact our supply and ability to provide staffing services to our customers. In addition, HCS may be charged higher insurance premiums for workers compensation and other corporate insurance coverage as a result of the COVID-19 pandemic. HCS may also be subject to claims regarding the health and safety of our staffed healthcare associates and our colleagues.

As HCS generates most of its revenue from customers which rely on the State of Georgia to provide them funding, the state may decrease the budgets for these services. As such, our CSB customers may need to scale back their programs and therefore reduce the employees we staff for them.

The foregoing and other potential disruptions to our business as a result of the COVID-19 pandemic could materially adversely affect our business and operating results, financial condition, and cash flow. The extent of such impact will depend on future developments, including the duration and spread of COVID-19, the speed at which the vaccine is distributed, the number of individuals in general who agree to receive the vaccine along with the number of our employees receiving the vaccine. In addition, the recent COVID-19 strain mutations may also hamper the vaccine's effectiveness.

The healthcare industry is highly regulated.

The healthcare industry is subject to extensive and complex federal, state and local laws and regulations related to, among other things, conduct of operations, and costs and payment for services. While HCS is not directly regulated as a healthcare provider, the customers of HCS are highly regulated. Therefore, HCS must comply with many of the regulations prescribed for its customers. If HCS does not comply with applicable laws and regulations, it could incur civil and/or criminal penalties as well as litigation or be subject to equitable remedies. HCS may lose customers if it cannot adequately adhere to the regulations.

HCS provides services to hospitals and health systems that pay HCS directly. Accordingly, Medicare, Medicaid and insurance reimbursement policy changes generally do not directly impact HCS. However, HCS's business, financial condition and results of operations depend upon conditions affecting the healthcare industry generally and hospitals and health systems particularly. The healthcare industry is highly regulated and is subject to changing political, economic and regulatory influences. Factors such as changes in reimbursement policies for healthcare expenses, consolidation in the healthcare industry, regulation, litigation and general economic conditions affect the purchasing practices, operations and the financial health of HCS's customers.

Reimbursement changes in government programs, particularly Medicare and Medicaid, can and do indirectly affect the demand and the prices paid for HCS's services. For example, HCS clients could receive reduced or no reimbursements because of a change in the rates or conditions set by the government, which would negatively affect the demand and the prices for HCS's services.

The business of HCS is concentrated in the State of Georgia and to a relatively few number of customers.

HCS derives all of its revenues from clients in the State of Georgia. As a result, HCS is subject to risks associated with conditions in the State of Georgia, including but not limited to economic and regulatory risks, than healthcare staffing and other companies that are more geographically diversified.

HCS derives the majority of its businesses from CSBs. There are 25 CSBs in Georgia and HCS conducts business with 12 of them. Matters that adversely impact Georgia CSBs, including regulatory changes, may negatively affect our business.

Our clients may terminate or not renew their contracts with us.

Our arrangements with CSBs and other customers generally are terminable upon 60 days' notice for any reason. The loss of one or more of our large customers could materially affect our profitability.

We may be unable to recruit enough healthcare professionals to meet our clients' demands.

HCS relies significantly on its ability to attract, develop and retain healthcare professionals who possess the skills, experience and, as required, licensure necessary to meet the specified requirements of our healthcare clients. The ability to recruit healthcare professionals generally and the competition for their services may limit our ability to increase the number of healthcare professionals that we successfully recruit, decreasing our ability to grow our business.

We are subject to litigation in the ordinary course of business, which could result in substantial judgment or settlement costs; significant legal actions could subject us to substantial uninsured liabilities.

HCS is a party to various litigation claims and legal proceedings in its normal course of business. We evaluate these litigation claims and legal proceedings to assess the likelihood of unfavorable outcomes and to estimate, if possible, the amount of potential losses. Actual outcomes or losses may differ materially from those estimated by our current assessments which would impact our profitability. Adverse developments in existing litigation claims or legal proceedings involving HCS or new claims could require us to establish litigation reserves, enter into unfavorable settlements or satisfy judgments for monetary damages for amounts in excess of current reserves, which could adversely affect our financial results. We may not have sufficient insurance to cover these risks. Litigation losses would impact our profitability.

Our collection, use, and retention of personal information and personal health information create risks that may harm our business.

As part of its business model, HCS collects, transmits and retains personal information of our employees and contract professionals and their dependents, including, without limitation, full names, social security numbers, addresses, birth dates, and payroll-related information. Employees or third parties may be able to circumvent security measures in place and acquire or misuse such information, resulting in breaches of privacy, and errors in the storage, use or transmission of such information may result in breaches of privacy. We may be required to incur significant expenses to comply with mandatory privacy and security standards and protocols imposed by law, regulation, industry standards, or contractual obligations if a privacy breach were to occur.

Cyber security risks and cyber incidents could adversely affect our business and disrupt operations.

Cyber incidents can result from deliberate attacks or unintentional events. These incidents can include, but are not limited to, gaining unauthorized access to digital systems for purposes of misappropriating assets or sensitive information, corrupting data, or causing operational disruption. The result of these incidents could include, but are not limited to, disrupted operations, misstated financial data, liability for stolen assets or information, increased cyber security protection costs, litigation and reputational damage adversely affecting customer or investor confidence. Security measures in place may not provide absolute security, and systems may be vulnerable to cyber-security breaches such as viruses, hacking, and similar disruptions from unauthorized intrusions. In addition, third party service providers perform certain services, such as payroll and tax services. Any failure of HCS or third party systems may compromise sensitive information and/or personally identifiable information of employees.

Risks Related to our Company

We have a history of operating losses and we may not generate sufficient revenue to support our operations.

During 2020, we had a net loss of $9.2 million. We also generated negative operating cash flow of $0.7 million. As of December 31, 2020, we had an overall shareholders deficit of $81.1 million. As of December 31, 2020, we had an aggregate of $1.3 million in cash and cash equivalents and total liabilities of $93.3 million. Of the $1.3 million in cash, $0.3 million was held by our subsidiary NMLLC. This cash is available only to pay general creditors and expenses of NMLLC.

From January 2019 through August 2019, the Company had a significant on-going obligation to pay interest under its senior note agreements at LIBOR plus 3.5% per annum, payable quarterly in arrears until maturity on March 30, 2033. The Company was successful in amending the senior note agreements to lower the interest rate and receive future credit for cash interest payments made in 2019 in exchange for the issuance of common stock and warrants. Based on the terms of the amendment, the Company is not required to make cash interest payments on the senior notes from August 2019 through March 2022. There is no cash interest payment due within one year from the date of the consolidated financial statements.

Management continues to work toward expanding HCS's customer base by increasing revenue from existing customers and targeting new customers that have not previously been served by HCS. In addition, management continues to explore cost cutting initiatives that will reduce overall overhead and operating costs, both at HCS and at the corporate level.

Our historical operating results and poor cash flow suggest substantial doubt exists related to the Company's ability to continue as a going concern. Furthermore, there is still significant uncertainty regarding the future impact that COVID-19 will have on our business. Based on these uncertainties, there is no guarantee the Company's cash position will cover current obligations. As a result, we have not been able to alleviate the substantial doubt about the Company's ability to continue as a going concern for at least one year after the date that these consolidated financial statements are issued.

We cannot provide assurance that revenue generated from our businesses will be sufficient to sustain our operations in the long term. Additionally, we cannot be certain that we will be successful at raising capital in the future. Such failures would have a material adverse effect on our business, including the possible cessation of operations.

We found material weaknesses in our disclosure controls and procedures and internal control over financial reporting and concluded that they were not effective as of December 31, 2020.

As disclosed in Part II, Item 9. Controls and Procedures of this Form 10-K, our chief executive officer and chief financial officer, with the participation of the Company's management, concluded that our disclosure controls and procedures and internal controls over financial reporting were not effective as of December 31, 2020 due to the lack of adequate processes, procedures and controls at HCS. Our failure to successfully remediate these material weaknesses could cause us to fail to meet our reporting obligations and to produce timely and reliable financial information. Additionally, such failure could cause investors to lose confidence in our public disclosures, which could have a negative impact on our stock price. For a discussion of these material weaknesses and our remediation efforts, see Part II, Item 9. Controls and Procedures of this Form 10-K.

Our ability to use our net operating loss carryforwards and net unrealized built-in losses could be severely limited.

As of December 31, 2020, we had federal net operating losses ("NOLs") of approximately $730.1 million, including $250.3 million in losses on mortgage securities that have not been recognized for income tax purposes. Our ability to use NOLs to offset future taxable income will depend on the amount of taxable income we generate in future periods and whether we become subject to annual limitations on the amount of taxable income that may be offset by our NOLs.

Section 382 of the Internal Revenue Code of 1986, as amended (the “Code”), imposes an annual limitation on the amount of taxable income that may be offset by a corporation’s NOLs if the corporation experiences an “ownership change” as defined in Section 382 of the Code. An ownership change occurs when the corporation’s “5-percent shareholders” (as defined in Section 382 of the Code) collectively increase their ownership in the corporation by more than 50 percentage points (by value) over a rolling three-year period. Additionally, various states have similar limitations on the use of state NOLs following an ownership change.

Our charter includes provisions designed to protect the tax benefits of our NOLs by generally restricting any direct or indirect transfers of our common stock that increase the direct or indirect ownership of our common stock by any person from less than 4.99% to 4.99% or more, or increase the percentage of our common stock owned directly or indirectly by a person owning or deemed to own 4.99% or more of our common stock. Any direct or indirect transfer attempted in violation of these transfer restrictions will be void as of the date of the prohibited transfer as to the purported transferee. These transfer restrictions expire on August 1, 2020. Additionally, we have adopted and our shareholders have approved a Rights Agreement (the “NOL Rights Plan”) that generally is designed to deter any person from acquiring shares of our common stock if the acquisition would result in such person beneficially owning 4.99% or more of our common stock without the approval of our Board of Directors (the “Board”). Shareholders voted to extend the NOL Rights Plan through July 20, 2021 at the Company's 2018 annual meeting of shareholders.

Although these measures are intended to reduce the likelihood of an ownership change, we cannot assure you that they will prevent all transfers of our common stock that could result in such an ownership change. Further, these measures could make it more difficult for a third party to acquire, or could discourage a third party from acquiring, the Company or a large block of our common stock, which may adversely affect the marketability, and depress the market price, of our common stock. In addition, these provisions could delay or frustrate the removal of incumbent directors and could make more difficult a merger, tender offer or proxy contest involving us, or impede an attempt to acquire a significant or controlling interest in us, even if such events might be beneficial to us and our shareholders.

Covenant restrictions under our indebtedness may limit our ability to operate our business.

The agreement governing the 2017 Notes contains, among other things, covenants that may restrict our and our subsidiaries' ability to finance future operations, capital needs or to engage in other business activities. The Note Purchase Agreement and the 2017 Notes limit our ability and the ability of our subsidiaries to take certain actions without the consent of the Noteholders, including but not limited to the following:

- incur indebtedness;
- create certain liens;
- make payments to our shareholders;
- acquire our outstanding shares, or the shares of our subsidiaries;
- make payments on debt securities junior to the 2017 Notes; and
- merge, consolidate, transfer and/or sell substantially all of our assets.

There can be no assurance that we will be able to receive the consent of the Noteholders should we have a need to take one of the restricted actions, which limitation may hinder our ability to operate or grow our business in the future.

Loss of key members of our management could disrupt our business.

The loss of key members of management could have a material adverse effect on our business, financial condition and results of operations. We may not be able to retain our existing senior management, fill new positions or vacancies created by expansion or turnover or attract additional qualified senior management personnel.

We may be required to repurchase mortgage loans or indemnify mortgage loan purchasers as a result of breaches of representations and warranties, borrower fraud, or certain borrower defaults, which could further harm our liquidity.

Prior to its acquisition of HCS, the Company originated, purchased, securitized, sold, invested in, and serviced residential nonconforming mortgage loans and mortgage securities. When we sold these mortgage loans, whether as whole loans or pursuant to a securitization, we made customary representations and warranties to the purchaser about the mortgage loans and the manner in which they were originated. Our whole loan sale agreements require us to repurchase or substitute mortgage loans in the event we breach any of these representations or warranties. In addition, we may be required to repurchase mortgage loans as a result of borrower, broker, or employee fraud. Likewise, we are required to repurchase or substitute mortgage loans if we breach a representation or warranty in connection with our securitizations. We have received various repurchase demands as performance of subprime mortgage loans has deteriorated. A majority of repurchase requests have been denied, otherwise a negotiated purchase price adjustment was agreed upon with the purchaser. Enforcement of repurchase obligations against us would further harm our liquidity.

Risks Related to our Capital Stock

There can be no assurance that our common stock will continue to be traded in an active market.

Our common stock currently trades on OTC Pink. Trading of securities on this quotation service is generally limited and is affected on a less regular basis than on exchanges, such as the NYSE, and accordingly investors who own or purchase our stock will find that the liquidity or transferability of the stock may be limited. Additionally, a shareholder may find it more difficult to dispose of, or obtain accurate quotations as to the market value of, our stock. If an active public trading market cannot be sustained, the trading price of our common stock could be adversely affected and the ability of an investor to transfer their shares of our common stock may be limited.

The market price and trading volume of our common stock may be volatile, which could result in substantial losses for our shareholders.

The market price of our capital stock can be highly volatile and subject to wide fluctuations. In addition, the trading volume in our capital stock may fluctuate and cause significant price variations to occur. Investors may experience volatile returns and material losses. Some of the factors that could negatively affect our share price or result in fluctuations in the price or trading volume of our capital stock include:
- actual or anticipated changes in our earnings and cash flow;
- general market and economic conditions, including the operations and stock performance of other industry participants;
- the impact of new state or federal legislation or adverse court decisions;
- sales, or the perception that sales could occur, of a substantial number of shares of our common stock by insiders;
- additions or departures of senior management and key personnel; and
- actions by institutional shareholders.

Some provisions of our charter, bylaws, Maryland law and our NOL Rights Plan may deter takeover attempts, which may limit the opportunity of our shareholders to sell their common stock at favorable prices.

Certain provisions of our charter, bylaws, Maryland law, and our NOL Rights Plan could discourage, delay or prevent transactions that involve an actual or threatened change in control, and may make it more difficult for a third party to acquire us, even if doing so may be beneficial to our shareholders. Under our charter, generally a director may only be removed for cause and only by the affirmative vote of the holders of at least a majority of all classes of shares entitled to vote in the election for directors together as a single class. Maryland law provides protection for Maryland corporations against unsolicited takeover situations. Further, our charter includes provisions designed to protect the tax benefits of our NOLs by generally restricting any direct or indirect transfers of our common stock that increase the direct or indirect ownership of our common stock by any person from less than 4.99% to 4.99% or more, or increase the percentage of our common stock owned directly or indirectly by a person owning or deemed to own 4.99% or more of our common stock. Any direct or indirect transfer attempted in violation of these transfer restrictions will be void as of the date of the prohibited transfer as to the purported transferee. These transfer restrictions expired on August 1, 2020. Additionally, we have adopted an NOL Rights Plan that generally is designed to deter any person from acquiring shares of our common stock if the acquisition would result in such person beneficially owning 4.99% or more of our common stock without the approval of our Board. Shareholders voted to extend the NOL Rights Plan through July 20, 2021 at the Company's 2018 annual meeting of shareholders.

Item 1B. Unresolved Staff Comments

None.

Item 2. Properties

The executive and administrative offices for the Company are located in Kansas City, Missouri, and consist of approximately 1,400 square feet of leased office space. HCS leases office space in a number of locations in the State of Georgia. The executive and administrative offices for HCS are located in College Park, Georgia, and consist of approximately 4,700 square feet of leased office space.

Item 3. Legal Proceedings

The Company is a party to various legal proceedings. These proceedings are of an ordinary and routine nature. For a discussion of material legal proceedings, see Note 7 to our consolidated financial statements included in Part II, Item 8 of this Annual Report on Form 10-K, which is incorporated herein by reference.

Item 4. Mine Safety Disclosures

None.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Company's common stock currently trades on OTC Pink under the symbol "NOVC". Prior to the commencement of the Company's Chapter 11 case, the Company's common stock traded on the OTCQB market of the OTC Markets Group, Inc. under the symbol "NOVC". There is no established public trading market for the Company's common stock. The following table sets forth the high and low bid prices as reported by these quotation services, for the periods indicated. The quotations represent inter-dealer prices without adjustment for retail markups, markdowns or commissions, and may not necessarily represent actual transactions.

	High	Low
2020		
First Quarter	$ 0.06	$ 0.03
Second Quarter	0.04	0.02
Third Quarter	0.07	0.02
Fourth Quarter	0.06	0.02
2019		
First Quarter	$ 0.08	$ 0.02
Second Quarter	0.07	0.02
Third Quarter	0.07	0.02
Fourth Quarter	0.06	0.02

As of February 25, 2021, we had approximately 696 shareholders of record of the Company's common stock. This figure does not represent the actual number of beneficial owners of our common stock because such stock is frequently held in "street name" by securities dealers and others for the benefit of individual owners who may vote the shares.

No dividends were declared during 2020 or 2019,nor do we expect to declare any stock dividend distributions in the near future. The Note Purchase Agreement governing the Company's senior notes contains restrictive covenants which prohibit the Company and its subsidiaries, from among other things, making any cash dividend or distribution to Novation shareholders. Should the restrictions be relieved, any future determination to pay dividends will be made at the discretion of our Board and will depend on earnings, financial condition, cost of equity, investment opportunities and other factors as our Board may deem relevant.

Item 6. Removed and Reserved

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following is a discussion and analysis of our financial condition and results of operations for the years ended December 31, 2020 and 2019. This discussion and analysis should be read in conjunction with our audited consolidated financial statements and Notes to the Consolidated Financial Statements set forth in Part II, Item 8, "Financial Statements and Supplementary Data" of this Form 10-K.

Corporate Overview

Through our wholly-owned subsidiary HCS, acquired on July 27, 2017, we provide outsourced health care staffing and related services in the State of Georgia. We also previously owned a portfolio of mortgage securities which generated earnings to support on-going financial obligations through the end of 2018. The mortgage securities were sold during 2018 for a total of $13.0 million. Our common stock, par value $0.01 per share, is traded on OTC Pink under the symbol "NOVC".

See Part I, Item 1 of this Form 10-K for a discussion of our note refinancing, which occurred in the third quarter of 2017, and the note amendment, which occurred in the third quarter of 2019.

Financial Highlights and Key Performance Metrics. The following key performance metrics (in thousands, except per share amounts) are derived from our consolidated financial statements for the periods presented and should be read in conjunction with the more detailed information therein and with the disclosure included in this report under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations."

	December 31,			
	2020		2019	
Cash and cash equivalents	$	1,340	$	2,032
Service fee income	$	51,354	$	63,474
General and administrative expenses	$	7,503	$	8,345
Net loss available to common shareholders, per basic share	$	(0.08)	$	(0.10)

Consolidated Results of Operations

Year Ended December 31, 2020 as Compared to the Year Ended December 31, 2019

Service Fee Income and Cost of Services

HCS delivers outsourced full-time and part-time employees primarily to Community Service Boards ("CSBs"), quasi state organizations that provide behavioral health services at facilities across Georgia including mental health services, developmental disabilities programs and substance abuse treatments. The State of Georgia has a total of 25 CSBs. Each CSB has a number of facilities, including crisis centers, outpatient centers and 24-hour group homes that require a broad range of employees, such as registered nurses, social workers, house parents and supervisors. The CSB market in Georgia is large and growing steadily, as the demand for the services provided by the CSBs continues to grow. In addition to providing outsourced employees to CSBs, HCS also provides healthcare outsourcing and staffing services to hospitals, schools and a variety of privately owned businesses. The services and positions provided to non-CSB clients are similar to the ones provided to CSB clients. The service fee income and costs of services in the consolidated statement of operations and comprehensive income (loss) are from the operations of HCS.

Future service fee income will be driven by the number of customers and the volume of associates employed by the CSB and outsourced to HCS. Customer contracts typically establish a fixed markup on the pay rate for the associates; therefore the cost of services will generally fluctuate consistently with fee income. HCS offers a health and welfare benefit plan to its associates. The cost of this benefit is passed through to CSB customers plus a small markup to cover the cost of administration.

A significant CSB customer terminated its contract services with HCS as of January 29, 2020. In addition, due to the recent developments of COVID-19, and the resulting reduction of programs and staff utilized by CSBs, the Company has experienced an impact to service fee income and cost of services starting in the second quarter of 2020 and continuing through the end of 2020.

General and Administrative Expenses

General and administrative expenses consist of salaries, office costs, legal and professional expenses and other customary costs of corporate administration. During 2020 and 2019, $5.5 and $6.2 million, respectively, of the total general and administrative expenses were incurred by HCS. Corporate-level general and administrative expenses during 2020 and 2019 were $2.0 million and $2.1 million, respectively. The future amount of corporate-level general and administrative expenses will depend largely on corporate activities and staffing needs based on the evolving business strategy. For HCS, the amount of these expenses will depend on business growth. Decreased marketing, advertising, and travel advertising expense along with reductions in corporate-level staffing are the primary reasons for the decrease in general and administrative expenses incurred by HCS.

Goodwill Impairment Charge

Management completed its annual goodwill impairment assessment as of April 30, 2020. Increased cost of services and administrative expenses at HCS and the loss of a significant customer during the first quarter of 2020 have resulted in declining cash flow for the business. In addition, COVID-19 concerns were attributable to a lay-off of staffed employees during the second quarter of 2020. Based on these factors, management determined that the carrying value of the HCS goodwill exceeded its fair value by the full amount recorded on the consolidated balance sheets of $3.9 million, as compared to fair value adjustments totaling $4.3 million in 2019. A goodwill impairment charge in this amount was recorded during the second quarter of 2020.

Interest Expense

Interest expense decreased period over period, with the Company incurring $3.3 million in 2020 and $4.5 million in 2019. See "Liquidity and Capital Resources" below and Note 6 to the consolidated financial statements for a discussion of the Note Purchase Agreement and the 2017 Notes, which were amended on August 9, 2019. The Amendment, among other things, significantly reduced the interest rate applicable from January 2019 through the third quarter of 2028.

Income Tax Expense

Because of the Company's significant net operating losses and full valuation allowance, income tax expense was not material for any period presented and is not expected to be material for the foreseeable future.

Liquidity and Capital Resources

During 2020, the Company had net loss of $9.2 million and generated negative operating cash flow of $0.7 million. As of December 31, 2020, the Company had an overall shareholders deficit of $81.1 million. As of December 31, 2020, the Company had an aggregate of $1.3 million in cash and cash equivalents and total liabilities of $93.3 million. Of the $1.3 million in cash, $0.3 million is held by the Company's subsidiary NMLLC. This cash is only available to pay general creditors and expenses of NMLLC.

Management continues to work toward expanding HCS's customer base by increasing revenue from existing customers, looking at methods to reduce overall operating costs, both at HCS and the corporate level, and targeting new customers that have not previously been served by HCS. As disclosed in Note 6 to the consolidated financial statements, the Company was successful in amending the senior note agreements to lower the interest rate and receive future credit for cash interest payments made in 2019 in exchange for the issuance of common stock and warrants. Based on the terms of the amendment, the Company is not required to make cash interest payments on the senior notes from August 2019 through March 2022, leading to significant cash savings for the Company. This amendment to the Note Purchase Agreement and waiver of interest payments through April 2022 has significantly improved our forecasted cash position over the next year.

In late March 2020, HCS started experiencing a reduction in Georgia CSB customer needs related to COVID-19. This resulted in the layoff of approximately 8% of the Company's employees. As HCS relies on providing healthcare staffing services to generate income, this has decreased our service fee income, and direct cost of services, accordingly. While the majority of these employees were rehired when customer demand returned, there have been some permanent loss of staffing opportunities based on changes to programs and services offered by CSBs. In addition, there is still concern at the Company about the ongoing effects of COVID-19 on our services for the foreseeable future. As of December 31, 2020, based on our operating losses and negative cash flow, substantial doubt exists related to the Company's ability to continue as a going concern.

Overview of Cash Flow for the Year Ended December 31, 2020

The following table provides a summary of our operating, investing and financing cash flows as taken from our consolidated statements of cash flows for the years ended December 31, 2020 and 2019 (in thousands).

	For the Years Ended December 31,	
	2020	**2019**
Cash flows used in operating activities	$ (677)	$ (5,168)
Cash flows (used in) provided by investing activities	(15)	(70)
Cash flows used in financing activities	—	(1,979)

Operating Activities

The decrease in net cash flows used in operating activities to approximately $0.7 million during 2020 from cash used in operating activities of $5.2 million during 2019 was driven primarily by the Company's decrease in net loss, along with a decrease in and paydowns of accounts receivable. Another contributor is the reduction of interest payments in 2020 resulting from the amendment of the senior note agreements, effective August 9, 2019.

Investing Activities

The decrease in the net cash flows used in investing activities is due to the reduction in purchases of property and equipment.

Financing Activities

The decrease in cash used in financing activities is due to the payoff of HCS's line of credit in 2019. The Company did not participate in any financing activities during 2020.

Critical Accounting Estimates

We prepare our consolidated financial statements in conformity with GAAP and, therefore, are required to make estimates regarding the values of our assets and liabilities and in recording income and expenses. These estimates are based, in part, on our judgment and assumptions regarding various economic conditions that we believe are reasonable based on facts and circumstances existing at the time of reporting. These estimates affect reported amounts of assets, liabilities and accumulated other comprehensive income at the date of the consolidated financial statements and the reported amounts of income, expenses and other comprehensive income during the periods presented. The following summarizes the components of our consolidated financial statements where understanding accounting policies is critical to understanding and evaluating our reported financial results, especially given the significant estimates used in applying the policies. The discussion is intended to demonstrate the significance of estimates to our consolidated financial statements and the related accounting policies. Management has discussed the development and selection of these critical accounting estimates with the Audit Committee of our Board and the Audit Committee has reviewed our disclosure.

Impairment of Indefinite-Lived Intangible Assets and Long-Lived Assets with Finite Lives

The values of indefinite-lived assets such as goodwill and trademarks are assessed annually to determine whether their carrying value exceeds their fair value. The Company performs its annual tests of goodwill and trademarks during the second quarter of each fiscal year. In addition, indefinite-lived assets are tested on an interim basis if an event occurs or circumstances change that would more likely than not reduce their fair value below carrying value and for long-lived purchased intangible assets this occurs whenever an event or circumstances indicate the carrying value of the asset may not be fully recoverable. If we determine the fair value of the asset is less than its carrying value, an impairment loss is recognized. Impairment losses, if any, are reflected in operating income or loss in the period incurred.

Income Taxes

In determining the amount of deferred tax assets to recognize in the consolidated financial statements, the Company evaluates the likelihood of realizing such benefits in future periods. The income tax guidance requires the recognition of a valuation allowance if it is more likely than not that all or some portion of the deferred tax asset will not be realized. Income tax guidance indicates the more likely than not threshold is a level of likelihood that is more than 50%.

Under the income tax guidance, companies are required to identify and consider all available evidence, both positive and negative, in determining whether it is more likely than not that all or some portion of its deferred tax assets will not be realized. Positive evidence includes, but is not limited to the following: cumulative earnings in recent years, earnings expected in future years, excess appreciated asset value over the tax basis and positive industry trends. Negative evidence includes, but is not limited to the following: cumulative losses in recent years, losses expected in future years, a history of operating losses or tax credit carryforwards expiring, and adverse industry trends.

The weight given to the potential effect of negative and positive evidence should be commensurate with the extent to which it can be objectively verified. The more negative evidence that exists, the more positive evidence is required to support a conclusion that a valuation allowance is not needed for all or some of the deferred tax assets. Cumulative losses in recent years are significant negative evidence that is difficult to overcome when determining the need for a valuation allowance. Similarly, cumulative earnings in recent years represent significant positive objective evidence. If the weight of the positive evidence is sufficient to support a conclusion that it is more likely than not that a deferred tax asset will be realized, a valuation allowance should not be recorded.

The Company examines and weighs all available evidence (both positive and negative and both historical and forecasted) in the process of determining whether it is more likely than not that a deferred tax asset will be realized. The Company considers the relevance of historical and forecasted evidence when there has been a significant change in circumstances. Additionally, the Company evaluates the realization of its recorded deferred tax assets on an interim and annual basis. The Company does not record a full valuation allowance if the weight of the positive evidence exceeds the negative evidence and is sufficient to support a conclusion that it is more likely than not that its deferred tax asset will be realized.

If a valuation allowance is necessary, the Company considers all sources of taxable income in determining the amount of valuation allowance to be recorded. Sources of taxable income identified in the income tax guidance include the following: 1) taxable income in prior carryback year, 2) future reversals of existing taxable temporary differences, 3) future taxable income exclusive of reversing temporary differences and carryforwards, and 4) tax planning strategies.

The Company currently evaluates estimates of uncertainty in income taxes based upon a framework established in the income tax accounting guidance. The guidance prescribes a recognition threshold and measurement standard for the recognition and measurement of tax positions taken or expected to be taken in a tax return. In accordance with the guidance, the Company evaluates whether a tax position will more likely than not be sustained upon examination by the appropriate taxing authority. The Company measures the amount to recognize in its consolidated financial statements as the largest amount that is greater than 50% likely of being realized upon ultimate settlement. The recognition and measurement of tax benefits is often judgmental, and determinations regarding the tax benefit can change as additional developments occur relative to the issue.

Impact of Recently Issued Accounting Pronouncements

No new accounting standards were adopted in 2020.

Item 7A. Quantitative and Qualitative Disclosures about Market Risk

Not applicable.

Item 8. Financial Statements and Supplementary Data

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

NOVATION COMPANIES, INC. AND SUBSIDIARIES

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Stockholders of Novation Companies, Inc.

Opinion on the Consolidated Financial Statements

We have audited the accompanying consolidated balance sheets of Novation Companies, Inc. (the Company) as of December 31, 2020 and 2019, and the related consolidated statements of operations and comprehensive income (loss), shareholders' deficit, and cash flows for each of the years in the two year period ended December 31, 2020, and the related notes (collectively referred to as the consolidated financial statements). In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2020 and 2019, and the results of its operations and its cash flows for each of the years in the two year period ended December 31, 2020, in conformity with accounting principles generally accepted in the United States of America.

Substantial Doubt About the Company's Ability to Continue as a Going Concern

The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 1 to the consolidated financial statements, the Company has incurred net operating losses and has had negative operating cash flow, combined with the impacts of COVID-19, this has led to substantial doubt related to the Company to continue as a going concern. Management's evaluation of the events and conditions and management's plans regarding those matters also are described in Note 1. The consolidated financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to that matter

Basis for Opinion

These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on the Company's consolidated financial statements based on our audits. We are a public accounting firm registered with the Public Company Accounting Oversight Board (United States) (PCAOB) and are required to be independent with respect to the Company in accordance with the U.S. federal securities laws and the applicable rules and regulations of the Securities and Exchange Commission and the PCAOB.

We conducted our audits in accordance with the standards of the PCAOB. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement, whether due to error or fraud. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. As part of our audits, we are required to obtain an understanding of internal control over financial reporting, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion.

Our audits included performing procedures to assess the risks of material misstatement of the consolidated financial statements, whether due to error or fraud, and performing procedures that respond to those risks. Such procedures included examining, on a test basis, evidence regarding the amounts and disclosures in the consolidated financial statements. Our audits also included evaluating the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that our audits provide a reasonable basis for our opinion.

Critical Audit Matters

The critical audit matters communicated below are matters arising from the current period audit of the consolidated financial statements that were communicated or required to be communicated to the audit committee and that: (1) relate to accounts or disclosures that are material to the consolidated financial statements and (2) involve especially challenging, subjective, or complex judgments. The communication of critical audit matters does not alter in any way our opinion on the consolidated financial statements, taken as a whole, and we are not, by communicating the critical audit matters below, providing separate opinions on the critical audit matters or on the accounts or disclosures to which they relate.

Valuation of Intangible Assets and Goodwill

Description of the Matter:

As disclosed in Notes 2 and 4 to the consolidated financial statements, the Company's intangible assets totaled $4.7 million at December 31, 2020 and goodwill was impaired by $3.9 million to its fair value of $0 during the second quarter of 2020. As disclosed in Note 2 to the consolidated financial statements, indefinite-lived intangible assets and goodwill are tested at least annually during the second quarter of each year. Finite-lived intangible assets are assessed for impairment whenever an event or change in circumstances indicates that the carrying value of the asset may not be recoverable. The Company determined that the onset of the COVID-19 pandemic and its negative effect on its service fee income was a triggering event that required an assessment of impairment for its finite-lived intangible assets.

Auditing the valuation of the Company's intangible assets and goodwill was highly judgmental due to the significant estimation required to determine the fair value of these assets as a result of the Company's current operating performance and the current industry and economic environment in which the Company operates. The Company's estimate of fair value for intangible assets and goodwill required significant judgment to estimate the impact of the decline in service fee income and profitability, industry trends, economic condition, including the impact of COVID-19, on future operating results and the future cash flows expected to be generated.

How We Addressed the Matter in Our Audit:

We obtained an understanding and evaluated the design of the controls related to the intangible asset and goodwill impairment assessment process, including controls over management's identification of indicators of impairment.

We performed audit procedures surrounding the impairment evaluation that included, among others, assessing methodologies and testing the significant assumptions and the completeness and accuracy of the underlying data used by the Company in its analysis. We reviewed management's discounted future cash flow analysis and the assessment of the assumptions used in this evaluation. We compared these assumptions prepared by management to current industry and economic trends, the Company's historical results, and other relevant factors.

/s/ BOULAY PLLP

We have served as the Company's auditor since 2016.

Minneapolis, Minnesota

March 4, 2021

NOVATION COMPANIES, INC.
CONSOLIDATED BALANCE SHEETS
(in thousands, except share and per share amounts)

	December 31, 2020	December 31, 2019
Assets		
Current assets:		
Cash and cash equivalents	$ 1,340	$ 2,032
Accounts and unbilled receivables	5,008	6,583
Prepaid expenses	663	647
Other	53	21
Total current assets	7,064	9,283
Non-current assets:		
Goodwill	—	3,905
Intangible assets, net	4,677	5,784
Property and equipment, net	92	125
Operating lease right-of-use asset	339	316
Other	4	4
Total non-current assets	5,112	10,134
Total assets	$ 12,176	$ 19,417
Liabilities and Shareholders' Deficit		
Current liabilities:		
Accounts payable and accrued expenses	$ 315	$ 524
Accrued compensation and benefits payable	2,176	2,717
Health and wellness program liability	—	492
Operating lease liability	195	205
Accrued claim settlements	246	246
Other	4	36
Total current liabilities	2,936	4,220
Non-current liabilities:		
Senior notes, net of unamortized debt premium of $4.2 million and $0.9 million as of December 31, 2020 and 2019, respectively	90,115	86,824
Accrued claim settlements	62	307
Operating lease liability	153	125
Total non-current liabilities	90,330	87,256
Total liabilities	93,266	91,476
Shareholders' deficit:		
Common stock, $.01 par value per share, 780,000,000 shares authorized: 114,655,893 and 112,355,893 shares issued and outstanding as of December 31, 2020 and 2019, respectively	1,146	1,123
Additional paid-in capital	746,227	746,112
Accumulated deficit	(828,463)	(819,294)
Total shareholders' deficit	(81,090)	(72,059)
Total liabilities and shareholders' deficit	$ 12,176	$ 19,417

See notes to consolidated financial statements.

NOVATION COMPANIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS
(in thousands, except share and per share amounts)

	For the Years Ended December 31, 2020	2019
Service fee income	$ 51,354	$ 63,474
Cost and expenses:		
Cost of services	45,819	56,483
General and administrative expenses	7,503	8,345
Goodwill impairment charge	3,905	4,300
Operating loss	(5,873)	(5,654)
Other income	43	39
Interest expense	(3,311)	(4,522)
Reorganization items, net	—	(63)
Loss before income taxes	(9,141)	(10,200)
Income tax expense	28	25
Net loss	(9,169)	(10,225)
Other comprehensive income:		
Unrealized gains on marketable securities	—	1
Total other comprehensive income	—	1
Total comprehensive loss	$ (9,169)	$ (10,224)
Loss per share:		
Basic	$ (0.08)	$ (0.10)
Diluted	$ (0.08)	$ (0.10)
Weighted average common shares outstanding:		
Basic	111,045,292	100,472,515
Diluted	111,045,292	100,472,515

See notes to consolidated financial statements.

NOVATION COMPANIES, INC.
CONSOLIDATED STATEMENTS OF SHAREHOLDERS' DEFICIT
(in thousands)

	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Shareholders' Deficit
Balance, December 31, 2019	$ 1,123	$ 746,112	$ (819,294)	$ —	$ (72,059)
Issuances of nonvested stock	23	(23)	—	—	—
Compensation recognized under stock compensation plans	—	138	—	—	138
Net loss	—	—	(9,169)	—	(9,169)
Balance, December 31, 2020	$ 1,146	$ 746,227	$ (828,463)	$ —	$ (81,090)

	Common Stock	Additional Paid-in Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Shareholders' Deficit
Balance, December 31, 2018	$ 991	$ 745,104	$ (809,050)	$ (1)	$ (62,956)
Issuances and cancellations of nonvested stock, net	42	(42)	—	—	—
Common stock granted in debt restructure	90	(90)	—	—	—
Common stock and common stock warrants granted in debt restructure	—	916	—	—	916
Compensation recognized under stock compensation plans	—	224	—	—	224
Net loss	—	—	(10,225)	—	(10,225)
Adjustment to retained earnings for adoption of accounting standard	—	—	(19)	—	(19)
Other comprehensive income	—	—	—	1	1
Balance, December 31, 2019	$ 1,123	$ 746,112	$ (819,294)	$ —	$ (72,059)

See notes to consolidated financial statements.

NOVATION COMPANIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands)

	For the Years Ended December 31, 2020	For the Years Ended December 31, 2019
Cash flows from operating activities:		
Net loss	$ (9,169)	$ (10,225)
Adjustments to reconcile net loss to net cash used in operating activities:		
Amortization of intangible assets	1,107	1,194
Amortization of debt premium and prepaid interest into interest expense	3,291	1,262
Depreciation expense	48	27
(Gain) loss on disposal of fixed assets	—	9
Lease expense	(5)	(5)
Goodwill impairment	3,905	4,300
Compensation recognized under stock compensation plans	138	224
Changes in operating assets and liabilities:		
Accounts and unbilled receivables	1,575	(461)
Accounts payable and accrued expenses	(209)	(146)
Accrued compensation and benefits payable	(541)	(14)
Accrued health and wellness program payable	(492)	492
Accrued interest payable	—	(754)
Accrued claim settlements	(245)	(459)
Other current assets and liabilities, net	(80)	(186)
Other noncurrent assets and liabilities, net	—	(426)
Net cash used in operating activities	(677)	(5,168)
Cash flows from investing activities:		
Purchases of property and equipment	(15)	(96)
Proceeds from sale of property and equipment	—	26
Net cash used in investing activities	(15)	(70)
Cash flows from financing activities:		
Borrowings under revolving line of credit	—	8,685
Repayments of borrowings under revolving line of credit	—	(10,633)
Paydowns of long-term debt	—	(31)
Net cash used in financing activities	—	(1,979)
Net decrease in cash and cash equivalents	(692)	(7,217)
Cash and cash equivalents, beginning of period	2,032	9,249
Cash and cash equivalents, end of period	$ 1,340	$ 2,032
Supplemental disclosure of cash flow information:		
Cash paid for interest	$ 21	$ 4,030
Cash paid for income taxes, net	$ 45	$ 30
Supplemental disclosure of non-cash investing and financing activities:		
Issuance of common stock in restructure of debt (Note 6)	$ —	$ 311
Issuance of common stock warrants in restructure of debt (Note 6)	$ —	$ 605

See notes to consolidated financial statements.

Note 1. Basis of Presentation, Business Plan and Liquidity

Description of Operations – Novation Companies, Inc. and its subsidiaries (the "Company," "Novation," "we," or "us"), through Healthcare Staffing, Inc. ("HCS"), our wholly-owned subsidiary acquired on July 27, 2017, provides outsourced health care staffing and related services in the State of Georgia. Our common stock, par value $0.01 per share, is traded on the OTC Pink marketplace of the OTC Markets Group, Inc. under the symbol "NOVC".

Liquidity and Going Concern – During 2020, the Company incurred a net loss of $9.2 million and generated negative operating cash flow of $0.7 million. As of December 31, 2020, the Company has an overall shareholders deficit of $81.1 million, an aggregate of $1.3 million in cash and cash equivalents and total liabilities of $93.3 million. Of the $1.3 million in cash, $0.3 million is held by the Company's subsidiary NovaStar Mortgage LLC ("NMLLC"). This cash is available only to pay only general creditors and expenses of NMLLC.

Prior to executing the Amendment with the Noteholders in August 2019 (Note 6), the Company had a significant on-going obligation to pay interest under its senior note agreements at LIBOR plus 3.5% per annum, payable quarterly in arrears until maturity on March 30, 2033, leading to a significant annual cash outflow. HCS has also experienced lower than anticipated cash flows in general due to increased costs and a decrease in business from certain customers. These items initially led to substantial doubt about the Company's ability to continue as a going concern.

Management continues to work toward expanding HCS's customer base by increasing revenue from existing customers, looking at methods to reduce overall operating costs, both at HCS and the corporate level, and targeting new customers that have not previously been served by HCS. As disclosed in Note 6 to the consolidated financial statements, the Company was successful in amending the senior note agreements to lower the interest rate and receive future credit for cash interest payments made in 2019 in exchange for the issuance of common stock and warrants. Based on the terms of the Amendment, the Company is not required to make cash interest payments on the senior notes from August 2019 through March 2022, leading to significant cash savings for the Company. This Amendment to the Note Purchase Agreement and waiver of interest payments through April 2022 has significantly improved our forecasted cash position over the next year.

In late March 2020, HCS started experiencing a reduction in CSB customer needs related to the COVID-19 pandemic. This resulted in the layoff of approximately 8% of the Company's employees. As HCS relies on providing healthcare staffing services to generate income, this has decreased our service fee income, and direct cost of services, accordingly. While the majority of these employees were rehired when customer demand returned, there have been some permanent loss of staffing opportunities based on changes to programs and services offered by CSBs. In addition, there is still concern at the Company about the ongoing effects of COVID-19 on our services for the foreseeable future.

Our historical operating results and negative cash flow suggest substantial doubt exists related to the Company's ability to continue as a going concern. Furthermore, there is still significant uncertainty regarding the future impact that COVID-19 will have on our business. Based on these uncertainties, there is no guarantee the Company's cash position will cover current obligations. As a result, we have not been able to alleviate the substantial doubt about the Company's ability to continue as a going concern for at least one year after the date that these condensed consolidated financial statements are issued.

Financial Statement Presentation. The Company's consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America ("GAAP"). The preparation of consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the consolidated financial statements and the reported amounts of income and expense during the period. The Company uses estimates and judgments in assessing the recoverability of its long-lived assets, impairments and accounting for income taxes, including the determination of the timing of the establishment or release of the valuation allowance related to the deferred tax asset balances and reserves for uncertain tax positions. While the consolidated financial statements and footnotes reflect the best estimates and judgments of management at the time, actual results could differ significantly from those estimates, and the amounts could be material.

Note 2. Summary of Significant Accounting and Reporting Policies

Cash and Cash Equivalents - Cash equivalents consist of liquid investments with an original maturity of three months or less. Cash equivalents are stated at cost, which approximates fair value. The Company maintains cash balances at four major financial institutions in the United States. Accounts are secured by the Federal Deposit Insurance Corporation up to $250,000. The uninsured balances of the Company's cash and cash equivalents accounts aggregated $0.8 million as of December 31, 2020.

Accounts and Unbilled Receivables - Accounts receivable are uncollateralized customer obligations due under normal trade terms. Customer account balances that are not paid within contract terms are considered delinquent. Accounts receivable are stated at the amount management expects to collect from outstanding balances. The Company maintains an allowance for potential losses primarily based upon management's analysis of delinquent accounts, routine assessment of its customers' financial condition, and any other known factors impacting collectability, including disputed amounts. When management has exhausted all collection efforts, amounts deemed uncollectible are written off. Recoveries of previously written off accounts receivable are recognized in the period in which they are received. The ultimate amount of accounts receivable that becomes uncollectible could differ from management's estimate.

Goodwill and Indefinite-Lived Intangible Assets - Goodwill and trademarks are assessed annually to determine whether their carrying value exceeds their fair value. In addition, they are tested on an interim basis if an event occurs or circumstances change between annual tests that would more likely than not reduce their fair value below carrying value. If we determine the fair value of goodwill or trademarks is less than their carrying value, an impairment loss is recognized. Impairment losses, if any, are reflected in operating income or loss in the period incurred. The Company performs its annual tests of goodwill and trademarks during the second quarter of each fiscal year.

Impairment of Long-Lived Intangible Assets with Finite Lives - Long-lived intangible assets held and used by us which have finite lives are assessed for impairment whenever an event or change in circumstances indicates that the carrying value of the asset may not be fully recoverable. Recoverability is determined based on an estimate of undiscounted future cash flows resulting from the use of an asset and its eventual disposition. An impairment loss is measured by comparing the fair value of the asset to its carrying value. If we determine the fair value of an asset is less than the carrying value, an impairment loss is incurred. Impairment losses, if any, are reflected in operating income or loss in the period incurred.

Revenue and Cost Recognition - The Company recognizes revenue when control of the promised services is transferred to customers and for the amount that reflects the consideration we are entitled to receive in exchange for those services. Furthermore, revenue is recognized at a point in time based on a fixed amount for each hour of staffing service provided as our customers benefit from our services and as we provide them. A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The Company's customer contracts have a single performance obligation to transfer the individual services, and it is not separately identifiable from other promises in the contracts and is, therefore, not distinct. Performance obligations are satisfied at the point in time the HCS employees work on behalf of the customer. Contract costs include compensation, benefits and overhead when appropriate. Because of the nature of the contracts and the fact that revenue is earned at the time the employee works for the customer, no contract estimates are necessary.

Income Taxes - The Company had a gross deferred tax asset of $168.8 million and $166.5 million as of December 31, 2020 and 2019, respectively. In determining the amount of deferred tax assets to recognize in the consolidated financial statements, the Company evaluates the likelihood of realizing such benefits in future periods. The income tax guidance requires the recognition of a valuation allowance if it is more likely than not that all or some portion of the deferred tax asset will not be realized. Income tax guidance indicates the more likely than not threshold is a level of likelihood that is more than 50%.

Under the income tax guidance, companies are required to identify and consider all available evidence, both positive and negative, in determining whether it is more likely than not that all or some portion of its deferred tax assets will not be realized. Positive evidence includes but is not limited to the following: cumulative earnings in recent years, earnings expected in future years, excess appreciated asset value over the tax basis and positive industry trends. Negative evidence includes but is not limited to the following: cumulative losses in recent years, losses expected in future years, a history of operating losses or tax credit carryforwards expiring, and adverse industry trends.

The weight given to the potential effect of negative and positive evidence should be commensurate with the extent to which it can be objectively verified. The more negative evidence that exists, the more positive evidence is required to support a conclusion that a valuation allowance is not needed for all or some of the deferred tax assets. Cumulative losses in recent years are significant negative evidence that is difficult to overcome when determining the need for a valuation allowance. Similarly, cumulative earnings in recent years represent significant positive objective evidence. If the weight of the positive evidence is sufficient to support a conclusion that it is more likely than not that a deferred tax asset will be realized, a valuation allowance should not be recorded.

The Company examines and weighs all available evidence (both positive and negative and both historical and forecasted) in the process of determining whether it is more likely than not that a deferred tax asset will be realized. The Company considers the relevance of historical and forecasted evidence when there has been a significant change in circumstances. Additionally, the Company evaluates the realization of its recorded deferred tax assets on an interim and annual basis. The Company does not record a full valuation allowance if the weight of the positive evidence exceeds the negative evidence and is sufficient to support a conclusion that it is more likely than not that its deferred tax asset will be realized.

If a valuation allowance is necessary, the Company considers all sources of taxable income in determining the amount of valuation allowance to be recorded. Sources of taxable income identified in the income tax guidance include the following: 1) taxable income in prior carryback year, 2) future reversals of existing taxable temporary differences, 3) future taxable income exclusive of reversing temporary differences and carryforwards, and 4) tax planning strategies.

The Company currently evaluates estimates of uncertainty in income taxes based upon a framework established in the income tax accounting guidance. The guidance prescribes a recognition threshold and measurement standard for the recognition and measurement of tax positions taken or expected to be taken in a tax return. In accordance with the guidance, the Company evaluates whether a tax position will more likely than not be sustained upon examination by the appropriate taxing authority. The Company measures the amount to recognize in its consolidated financial statements as the largest amount that is greater than 50% likely of being realized upon ultimate settlement. The recognition and measurement of tax benefits is often judgmental, and determinations regarding the tax benefit can change as additional developments occur relative to the issue.

Earnings (Loss) Per Share ("EPS") - Basic EPS excludes dilution and is computed by dividing net income (loss) available to common shareholders by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock or resulted in the issuance of common stock that then shared in the earnings of the entity. Diluted EPS is calculated assuming all options, nonvested shares and performance-based awards of the Company's common stock have been exercised, unless the exercise would be antidilutive.

Segments - The Company has evaluated it's operations and determined it has one reportable segment.

Note 3. Revenue; Accounts and Unbilled Receivables

Staffing services include the augmentation of customers' workforce with our contingent employees performing services under the customers' supervision, which provides our customers with a source of flexible labor at a competitive cost. Customer contracts are typically annual contracts but may be terminated upon 60 days' notice for any reason.

The Company recognizes revenue when control of the promised services is transferred to customers and for the amount that reflects the consideration we are entitled to receive in exchange for those services. Furthermore, revenue is recognized over time based on a fixed amount for each hour of staffing service provided as our customers benefit from our services and as we provide them.

Performance Obligations — A performance obligation is a promise in a contract to transfer a distinct good or service to the customer. A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. The Company's customer contracts have a single performance obligation to transfer the individual goods or services, and it is not separately identifiable from other promises in the contracts and is, therefore, not distinct. Performance obligations are satisfied at the point in time the HCS employees work on behalf of the customer. Contract costs include compensation, benefits and overhead when appropriate. Because of the nature of the contracts and the fact that revenue is earned at the time the employee works for the customer, no contract estimates are necessary.

Contract Balances — The timing of revenue recognition, billings and cash collections results in accounts receivable and unbilled receivables (the "contract assets"). The Company bills customers generally every other week based on the work performed during the two-week period ended the week prior to billing. Generally, billing occurs after revenue recognition, resulting in contract assets. The Company does not receive advances or deposits from its customers.

Disaggregation of Revenue — All revenue is generated from customers that provide healthcare services in Georgia. The following is a disaggregation of the Company's revenue, in thousands, into categories that best depict how the nature, amount, timing, and uncertainty of revenues and cash flows are affected by economic factors.

	For the Year Ended December 31, 2020		For the Year Ended December 31, 2019	
Type of Customer				
CSB	$ 50,054	97.5%	$ 61,620	97.1%
Other	1,300	2.5%	1,854	2.9%
Total	$ 51,354	100.0%	$ 63,474	100.0%

Accounts and unbilled receivables are summarized as follows, in thousands:

	December 31, 2020	December 31, 2019
Accounts receivable	$ 2,705	$ 4,083
Unbilled receivables (Contract Assets)	2,303	2,500
Total accounts and unbilled receivables	$ 5,008	$ 6,583

As of December 31, 2020 and December 31, 2019, management has determined no allowance for doubtful accounts is necessary. For the years ended December 31, 2020 and December 31, 2019, 63.3% and 63.1% of service fee income was generated from four customers. As of December 31, 2020, 64.0% of accounts and unbilled receivables was due from four customers and 88.8% was due from 12 CSB customers. As of December 31, 2019, 61.6% of accounts and unbilled receivables was due from four customers and 96.6% was due from 14 CSB customers.

Note 4. Goodwill and Intangible Assets

	December 31, 2020			December 31, 2019		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Indefinite-lived assets (in thousands):						
Goodwill	$ —	$ —	$ —	$ 3,905	$ —	$ 3,905
Tradenames	1,147	—	1,147	1,147	—	1,147
Total indefinite-lived assets	$ 1,147	$ —	$ 1,147	$ 5,052	$ —	$ 5,052
Finite-lived assets (in thousands):						
Customer relationships	$ 6,895	$ 3,365	$ 3,530	$ 6,895	$ 2,380	$ 4,515
Non-compete agreement	627	627	—	627	505	122
Total finite-lived assets	$ 7,522	$ 3,992	$ 3,530	$ 7,522	$ 2,885	$ 4,637

Amortization expense (in thousands):	
2019	$ 1,194
2020	1,107
Estimated future amortization expense (in thousands):	
2021	$ 985
2022	985
2023	985
Thereafter	575
Total estimated amortization expense	$ 3,530

	Years Ended December 31,	
	2020	2019
Goodwill activity (in thousands):		
Beginning balance	$ 3,905	$ 8,205
Impairment charge	(3,905)	(4,300)
Ending balance	$ —	$ 3,905

Management completed its annual goodwill impairment assessment as of April 30, 2020. Increased cost of services and administrative expenses at HCS and the loss of a significant customer during the first quarter of 2020 have resulted in declining cash flow for the business. In addition, COVID-19 concerns were attributable to a lay-off of staffed employees starting in the second quarter of 2020. Based on these factors, management determined that the carrying value of the HCS goodwill exceeded its fair value by the full amount recorded on the consolidated balance sheets of $3.9 million. A goodwill impairment charge in this amount was recorded during the second quarter of 2020. Management assessed the other indefinite and definite lived intangible assets and determined no impairment was necessary.

Note 5. Leases

Our leases consist primarily of office space. Leases with an initial term of 12 months or less, and leases which are on a month-to-month basis, are not recorded on the balance sheet. For these leases we recognize lease expense on a straight-line basis over the lease term. The Company does not have any finance leases.

Most leases include one or more options to renew, with renewal terms that can extend the lease term from one to three years or more. The exercise of lease renewal options is at our discretion. Our lease agreements do not contain any variable lease payments, residual value guarantees or restrictive covenants. The components of lease expense for the twelve months ended December 31, 2020 were immaterial. As our leases do not provide an implicit interest rate, we use our incremental current borrowing rate in determining the present value of lease payments.

Maturities of lease liabilities were as follows (in thousands):

	December 31, 2020
2021	$ 212
2022	88
2023	57
Thereafter	19
Total	$ 376
Less interest	28
Present value of lease liabilities	$ 348

Other information related to the Company's operating leases was as follows (in thousands):

	December 31, 2020
Lease Term and Discount Rate:	
Weighted average remaining lease term (years)	2.20
Weighted average discount rate	6.75%

Note 6. Borrowings

Note Refinancing and 2017 Notes — On August 9, 2019, the Company and Taberna Preferred Funding I, Ltd. (“Taberna I”), Taberna Preferred Funding II, Ltd. (“Taberna II”) and Kodiak CDO I, Ltd. (“Kodiak” and, together with Taberna I and Taberna II, the “Noteholders”) executed a First Amendment to Senior Secured Note Purchase Agreement (the “Amendment”) amending the terms of the Note Purchase Agreement (as defined below) and the 2017 Notes (as defined below) to, among other things, significantly reduce the interest rate applicable from January 2019 through the third quarter of 2028 and allow the Company to apply certain surplus interest payments against future quarterly interest payments. This amendment qualified as a troubled debt restructuring. As of December 31, 2020, the Company had $85.9 million in aggregate borrowings outstanding under three senior secured promissory notes (the “2017 Notes”). The unpaid principal amounts of the 2017 Notes bear interest at the following rates until the maturity date on March 30, 2033, with interest payable quarterly in arrears as follows: 1% per annum from April 1, 2019 through December 31, 2023; 2% per annum from January 1, 2024 through December 31, 2028; and 10% per annum from January 1, 2029 through the maturity date. Commencing with the delivery to the Noteholders of the financial statements for the fiscal year ending December 31, 2019, the Company is required to remit 50% of excess cash flow each year to the Noteholders to be applied as a principal reduction to the outstanding balance of the debt. The 2017 Notes generally rank senior in right of payment to any existing or future subordinated indebtedness of the Credit Parties (as defined below). The Company may at any time upon 30 days’ notice to the Noteholders redeem all or part of the 2017 Notes at a redemption price equal to 101% of the principal amount redeemed plus any accrued and unpaid interest thereon. The 2017 Notes were entered into on July 27, 2017 as a result of a refinancing of the Company’s then outstanding senior notes with the same aggregate principal amount through the execution of the Senior Secured Note Purchase Agreement, dated as of the same date (as amended, the “Note Purchase Agreement”), with Novation Holding, Inc., a wholly-owned subsidiary of the Company ("NHI") and HCS as guarantors (together with the Company, collectively, the “Credit Parties”).

On April 1, 2019 and on July 1, 2019, the Company made payments under the 2017 Notes totaling $2.6 million. The actual aggregate amounts due for those dates totaled $0.4 million. Under the terms of the Amendment, the Company is permitted to apply the payment surplus of $2.2 million against future quarterly interest payments. Therefore, the Company will not have another quarterly interest payment due until April 1, 2022. The Note Purchase Agreement contains customary affirmative and negative covenants, including but not limited to certain financial covenants. Under the terms of the Amendment, the financial covenants have been waived until the quarter ending December 31, 2021. The Note Purchase Agreement also contains customary events of default, including but not limited to payment defaults, cross defaults with certain other indebtedness, breaches of covenants and bankruptcy events. In the case of an event of default, the Noteholders may, among other remedies, accelerate the payment of all obligations under the Note Purchase Agreement and the 2017 Notes. The Credit Parties entered into a Pledge and Security Agreement, dated as of the same date, pursuant to which each of the Credit Parties granted a first priority lien generally covering all of its assets, other than accounts receivable and inventory, for the benefit of the Noteholders, to secure the obligations under the Note Purchase Agreement and the 2017 Notes.

Under the terms of the Amendment, the Company issued to the Noteholders 9,000,000 shares of common stock of the Company and ten-year warrants allowing the Noteholders to purchase up to 22,250,000 shares of the Company's common stock at an exercise price of $0.01 per share. These warrants can be exercised at any time prior to expiration. At the time of the Amendment, the outstanding principal balance of the notes were reduced by the fair value of the common stock and warrants issued by the Company, resulting in debt premium of $0.9 million, offset by accrued interest of $0.5 million. The Company will amortize the debt premium and prepaid interest over the amended term of the Note Purchase Agreement using the effective interest method. Under the effective interest method, significant changes in the rate at which a debt instrument accrues interest over its term can result in a recorded balance in excess of the aggregate principal balance of the debt instrument.

The carrying value of the 2017 Notes is as follows (in thousands):

	December 31, 2020	December 31, 2019
Principal balance	$ 85,938	$ 85,938
Unamortized debt premium	4,177	886
Total, 2017 Notes	$ 90,115	$ 86,824

Note 7. Commitments and Contingencies

Contingencies. Prior to 2016, the Company originated, purchased, securitized, sold, invested in and serviced residential nonconforming mortgage loans and mortgage securities. The Company has received indemnification and loan repurchase demands with respect to alleged violations of representations and warranties ("defects") and with respect to other alleged misrepresentations and contractual commitments made in loan sale and securitization agreements. These demands have been received substantially beginning in 2006 and have continued into recent years. Prior to the Company ceasing the origination of loans in its mortgage lending business, it sold loans to securitization trusts and other third parties and agreed to repurchase loans with material defects and to otherwise indemnify parties to these transactions. Beginning in 1997 and ending in 2007, affiliates of the Company sold loans to securitization trusts and third parties with the potential of such obligations. The aggregate original principal balance of these loans was $43.1 billion at the time of sale or securitization. The remaining principal balance of these loans is not available as these loans are serviced by third parties and may have been refinanced, sold or liquidated. Claims to repurchase loans or to indemnify under securitization documents have not been acknowledged as valid by the Company. In some cases, claims were made against affiliates of the Company that have ceased operations and have no or limited assets. The Company has not repurchased any loans or made any such indemnification payments since 2010.

Historically, repurchases of loans or indemnification of losses where a loan defect has been alleged have been insignificant and any future losses for alleged loan defects have not been deemed to be probable or reasonably estimable; therefore, the Company has recorded no reserves related to these claims. The Company does not use internal groupings for purposes of determining the status of these loans. The Company is unable to develop an estimate of the maximum potential amount of future payments related to repurchase demands because the Company does not have access to information relating to loans sold and securitized and the number or amount of claims deemed probable of assertion is not known nor is it reasonably estimated. Further, the validity of claims received remains questionable. Also, considering that the Company completed its last sale or securitization of loans during 2007, the Company believes that it will be difficult for a claimant to successfully validate any additional repurchase demands. Management does not expect that the potential impact of claims will be material to the Company's consolidated financial statements.

Pending Litigation. The Company is a party to various legal proceedings. Except as set forth below, these proceedings are of an ordinary and routine nature. Any legal fees associated with these proceedings are expensed as incurred.

Although it is not possible to predict the outcome of any legal proceeding, in the opinion of management, other than the active proceedings described in detail below, proceedings and actions against the Company should not, individually, or in the aggregate, have a material effect on the Company's financial condition, operations and liquidity. Furthermore, due to the uncertainty of any potential loss as a result of pending litigation and due to the Company's belief that an adverse ruling is not probable, the Company has not accrued a loss contingency related to the following matters in its consolidated financial statements. However, a material outcome in one or more of the active proceedings described below could have a material impact on the results of operations in a particular quarter or fiscal year.

On May 21, 2008, a purported class action case was filed in the Supreme Court of the State of New York, New York County, by the New Jersey Carpenters' Health Fund, on behalf of itself and all others similarly situated. Defendants in the case included NMFC and NovaStar Mortgage, Inc. ("NMI"), wholly-owned subsidiaries of the Company, and NMFC's individual directors, several securitization trusts sponsored by the Company (“affiliated defendants”) and several unaffiliated investment banks and credit rating agencies. The case was removed to the United States District Court for the Southern District of New York. On June 16, 2009, the plaintiff filed an amended complaint. The plaintiff seeks monetary damages, alleging that the defendants violated sections 11, 12 and 15 of the Securities Act of 1933, as amended, by making allegedly false statements regarding mortgage loans that served as collateral for securities purchased by the plaintiff and the purported class members. On August 31, 2009, the Company filed a motion to dismiss the plaintiff's claims, which the court granted on March 31, 2011, with leave to amend. The plaintiff filed a second amended complaint on May 16, 2011, and the Company again filed a motion to dismiss. On March 29, 2012, the court dismissed the plaintiff's second amended complaint with prejudice and without leave to replead. The plaintiff filed an appeal. On March 1, 2013, the appellate court reversed the judgment of the lower court, which had dismissed the case. Also, the appellate court vacated the judgment of the lower court which had held that the plaintiff lacked standing, even as a class representative, to sue on behalf of investors in securities in which plaintiff had not invested, and the appellate court remanded the case back to the lower court for further proceedings. On April 23, 2013 the plaintiff filed its memorandum with the lower court seeking a reconsideration of the earlier dismissal of plaintiff's claims as to five offerings in which plaintiff was not invested, and on February 5, 2015 the lower court granted plaintiff's motion for reconsideration and vacated its earlier dismissal. On March 8, 2017, the affiliated defendants and all other parties executed an agreement to settle the action, with the contribution of the affiliated defendants to the settlement fund being paid by their insurance carriers. The court certified a settlement class and granted preliminary approval to the settlement on May 10, 2017. One member of the settlement class objected to the settlement and sought a stay of the final settlement approval hearing on the ground that it did not receive notice of the settlement and had no opportunity to timely opt out of the class. After the court rejected the motion for a stay, the objector filed an appeal and requested a stay of the district court proceedings pending disposition of the appeal. The court of appeals denied the temporary stay of the district court proceedings and on October 19, 2018 dismissed the appeal as moot. Following the court of appeals’ denial of the objector’s petition for rehearing, the district court on March 7, 2019 held a fairness hearing. On March 8, 2019, the district court issued a memorandum and order approving the settlement as fair, reasonable and adequate, and dismissing the action with prejudice. Following entry of judgment, the objector filed a notice of appeal on March 26, 2019 and their opening brief was filed on June 28, 2019. The defendants answered on September 27, 2019, and the objector replied on October 18, 2019. Oral argument was held on February 19, 2020. Assuming the settlement approval becomes final, which is expected, the Company will incur no loss. The Company believes that the Affiliated Defendants have meritorious defenses to the case and, if the settlement approval does not become final, expects them to defend the case vigorously.

On June 20, 2011, the National Credit Union Administration Board, as liquidating agent of U.S. Central Federal Credit Union, filed an action against NMFC and numerous other defendants in the United States District Court for the District of Kansas, claiming that the defendants issued or underwrote residential mortgage-backed securities pursuant to allegedly false or misleading registration statements, prospectuses, and/or prospectus supplements. On August 24, 2012, the plaintiff filed an amended complaint making essentially the same claims against NMFC. NMFC filed a motion to dismiss the amended complaint which was denied on September 12, 2013. The defendants had claimed that the case should be dismissed based upon a statute of limitations and sought an appeal of the court's denial of this defense. An interlocutory appeal of this issue was allowed, and on August 27, 2013, the Tenth Circuit affirmed the lower court’s denial of defendants’ motion to dismiss the plaintiff’s claims as being time barred; the appellate court held that the Extender Statute, 12 U.S.C. §1787(b)(14) applied to plaintiff’s claims. On June 16, 2014, the United States Supreme Court granted a petition of NMFC and its co-defendants for certiorari, vacated the ruling of the Tenth Circuit, and remanded the case back to that court for further consideration in light of the Supreme Court’s decision in CTS Corp. v. Waldburger, 134 S. Ct. 2175 (2014). On August 19, 2014, the Tenth Circuit reaffirmed its prior decision, and on October 2, 2014 the defendants filed a petition for writ of certiorari with the Supreme Court, which was denied. On March 22, 2016, NMFC filed motions for summary judgment, and plaintiff filed a motion for partial summary judgment. The case was stayed after NMFC filed a bankruptcy case. On September 2, 2020, the parties filed a stipulation of dismissal with prejudice and the case was terminated by the Court**.**

On February 28, 2013, the Federal Housing Finance Agency, as conservator for the Federal Home Loan Mortgage Corporation (Freddie Mac) and purportedly on behalf of the Trustee of the NovaStar Mortgage Funding Trust, Series 2007-1 (the “Trust”), a securitization trust in which the Company retains a residual interest, filed a summons with notice in the Supreme Court of the State of New York, New York County against the Company and NMI. The notice provides that this is a breach of contract action with respect to certain, unspecified mortgage loans and defendants’ failure to repurchase such loans under the applicable agreements. Plaintiff alleges that defendants, from the closing date of the transaction that created the Trust, were aware of the breach of the representations and warranties made and failed to give notice of and cure such breaches, and due to the failure of defendants to cure any breach, notice to defendants would have been futile. Eventually, the parties reached a settlement of this matter, which required an upfront payment of $0.3 million and equal quarterly installments over three years totaling an additional $0.3 million.

DB Structured Products, Inc., Deutsche Bank AG, Deutsche Bank National Trust Company, Deutsche Bank Securities Inc., Greenwich Capital Derivatives, Inc., RBS Acceptance Inc., RBS Financial Products Inc., RBS Securities Inc., The Royal Bank of Scotland PLC, Wachovia Investment Holdings, LLC, Wells Fargo & Company, Wells Fargo Advisors, LLC, Wells Fargo Bank, N.A. and Wells Fargo Securities, LLC (collectively, the “Indemnity Claimants”) filed proofs of claim in the Company’s bankruptcy case asserting the right to be indemnified by the Company for, and/or to receive contribution from the company in respect of, certain liabilities incurred as a result of their roles in the issuance of residential mortgage-backed securities sponsored by the Company. Eventually, the parties reached a settlement in this matter, which required an upfront payment of $0.5 million and equal quarterly installments over three years totaling an additional $0.4 million.

Note 8. Fair Value Accounting

Fair Value Measurements

The Company's valuation techniques are based upon observable and unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs create the following fair value hierarchy:

- Level 1 – Valuations based on quoted prices in active markets for identical assets and liabilities.
- Level 2 – Valuations based on observable inputs in active markets for similar assets and liabilities, other than Level 1 prices, such as quoted interest or currency exchange rates for substantially the full term of the asset or liability.
- Level 3 – Valuations based on significant unobservable inputs that are supported by little or no market activity, such as discounted cash flow methodologies based on internal cash flow forecasts.

The following table provides the estimated fair value of financial instruments and presents amounts that have been determined using available market information and appropriate valuation methodologies. However, considerable judgment is required to interpret market data to develop the estimates of fair value. Accordingly, the estimates presented herein are not necessarily indicative of the amounts that could be realized in a current market exchange. The use of different market assumptions or estimation methodologies could have a material impact on the estimated fair value amounts. The fair value of short-term financial assets and liabilities, such as service fees receivable, notes receivable, and accounts payable and accrued expenses are not included in the following table as their carrying value approximates their fair value.

The estimated fair values of the Company's financial instruments are as follows as of December 31, 2020 and 2019 (in thousands):

	December 31, 2020		December 31, 2019	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial liabilities:				
2017 Notes (Level 3)	$ 90,115	$ 11,365	$ 86,824	$ 21,289

The 2017 Notes in the table above are not measured at fair value in the consolidated balance sheets but are required to be disclosed at fair value. The fair value of the 2017 Notes has been estimated using Level 3 methodologies, based on significant unobservable inputs that are supported by little or no market activity, such as discounted cash flow calculations based on internal cash flow forecasts. No assets or liabilities have been transferred between levels during any period presented. The fair value is estimated by discounting future projected cash flows using a discount rate commensurate with the risks involved. The interest rate on the senior notes is 1% per annum from April 1, 2019 through December 31, 2023; 2% per annum from January 1, 2024 through December 31, 2028; and 10% per annum from January 1, 2029 through the maturity date in March 2033.

Goodwill — See Note 4 to the consolidated financial statements for more information on the goodwill impairment assessments performed in 2020.

Assets reported at fair value on a nonrecurring basis include the following (in thousands):

	December 31, 2020	
	Fair Value (Level 3)	Gains and (Losses)
Goodwill	$ —	$ (3,905)

Activity during 2020 for Goodwill, the Company's only Level 3 asset, measured on a nonrecurring basis is included in the following table (in thousands):

Goodwill Activity:	
Balance, December 31, 2019	$ 3,905
Impairment charge	(3,905)
Balance, December 31, 2020	$ —

The determination of the goodwill impairment was based on a discounted cash flow approach utilizing forecasted revenue ranging from $57 million to $69 million, historical operating income percentages, and a cost of capital of approximately 15%.

Prior to the Company's acquisition of HCS in 2017, the Company originated, purchased, securitized, sold, invested in and serviced residential nonconforming mortgage loans and mortgage securities. The Company retains clean-up call rights associated with prior servicing activities and has determined these clean-up call rights have no fair value as of December 31, 2020 and 2019.

Note 9. Income Taxes

The components of income tax expense (benefit) from continuing operations are (in thousands):

	For the Years Ended December 31,	
	2020	2019
Current:		
Federal	$ —	$ (11)
State and local	28	36
Total current	$ 28	$ 25

Below is a reconciliation of the expected federal income tax expense (benefit) using the federal statutory tax rate of 21% to the Company's actual income tax expense (benefit) and resulting effective tax rate (in thousands).

	For the Years Ended December 31,	
	2020	2019
Income tax benefit at statutory rate	$ (1,926)	$ (2,949)
State income taxes, net of federal tax benefit	(71)	36
Valuation allowance	2,278	2,528
Bankruptcy reorganization	—	9
Other	(253)	401
Total income tax expense	$ 28	$ 25

Prior to 2019, the Company concluded that it was no longer more likely than not that it would realize a portion of its deferred tax assets. As such, the Company maintained a full valuation allowance against its net deferred tax assets as of both December 31, 2020 and 2019.

The Company's determination of the realizable deferred tax assets requires the exercise of significant judgment, based in part on business plans and expectations about future outcomes. In the event the actual results differ from these estimates in future periods, the Company may need to adjust the valuation allowance, which could materially impact our financial position and results of operations. The Company will continue to assess the need for a valuation allowance in future periods. As of December 31, 2020 and 2019, the Company maintained a valuation allowance of $168.8 million and $166.5 million, respectively, for its deferred tax assets.

Significant components of the Company's deferred tax assets and liabilities as of December 31, 2020 and 2019 are (in thousands):

	December 31,	
	2020	2019
Deferred tax assets:		
Federal NOL carryforwards	$ 153,320	$ 152,705
State NOL carryforwards	9,044	9,003
Goodwill impairment, HCS	2,069	1,084
Business interest expense limitation	2,578	1,877
Other	1,812	1,876
Gross deferred tax asset	168,823	166,545
Valuation allowance	(168,823)	(166,545)
Deferred tax asset	—	—
Deferred tax liabilities:		
Other	—	—
Deferred tax liability	—	—
Net deferred tax asset	$ —	$ —

The other deferred tax assets consist of differences in various accrued expenses, debt restructuring expenses, goodwill and intangible asset book to tax differences, and various other book to tax differences.

As of December 31, 2020, the Company had a federal NOL of approximately $730.1 million, including $250.3 million in losses on mortgage securities that have not been recognized for income tax purposes. The federal NOL may be carried forward to offset future taxable income, subject to applicable provisions of the Internal Revenue Code (the "Code"). If not used, these NOLs will expire in years 2025 through 2037. Due to tax reform enacted in 2017, NOLs created after 2017 carry forward indefinitely; the portion of NOLs that will not expire is $94.9 million. The Company has state NOL carryforwards arising from both combined and separate filings from as early as 2004. The state NOL carryforwards may expire as early as 2019 and as late as 2037.

The activity in the accrued liability for unrecognized tax benefits for the years ended December 31, 2020 and 2019 was (in thousands):

	For the Years Ended December 31,	
	2020	2019
Beginning balance	$ —	$ 11
Gross increases – tax positions in current period	—	—
Lapse of statute of limitations	—	(11)
Ending balance	$ —	$ —

Accounting for income taxes, including uncertain tax positions, represents management's best estimate of various events and transactions, and requires significant judgment. As of December 31, 2020 and 2019. there were no unrecognized tax benefits. The Company does not expect any other significant change in the liability for unrecognized tax benefits in the next twelve months. It is the Company’s policy to recognize interest and penalties related to income tax matters in income tax expense. The benefit for interest and penalties recorded in income tax expense was not significant for 2020 and 2019. There were accrued interest and penalties of less than $0.1 million as of both December 31, 2020 and 2019. The Company and its subsidiaries are subject to U.S. federal income tax as well as income tax of multiple state and local jurisdictions. Tax years 2017 to 2020 remain open to examination for both U.S. federal income tax and major state tax jurisdictions.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, our chief executive officer and our chief financial officer conducted an evaluation of the effectiveness of the design and operation of our 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")). Based on their evaluation of our disclosure controls and procedures, our chief executive officer and chief financial officer, with the participation of the Company's management, concluded that our disclosure controls and procedures were not effective as of December 31, 2020, to ensure that information required to be disclosed by the Company in the reports that we file or submit under the Exchange Act is (a) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms and (b) accumulated and communicated to management, including our principal executive officer and principal financial officer, as appropriate to allow for timely decisions regarding required disclosure.

Management's Annual Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal control over financial reporting as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. Our internal control over financial reporting is designed to provide reasonable assurance regarding the reliability of our financial reporting and the preparation of consolidated financial statements for external purposes in accordance with GAAP. Under the supervision and with the participation of management, including the Company's principal executive officer and principal financial officer, the Company conducted an evaluation of the effectiveness of its internal control over financial reporting as of December 31, 2020 based on the framework set forth in Internal Control—Integrated Framework (2013), issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on that evaluation and its assessment, management concluded that the Company's internal control over financial reporting was not effective as of December 31, 2020.

Description of Material Weakness of Disclosure Controls

As discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations above, in July 2017, we acquired HCS, which now is our primary business activity. Prior to the HCS Acquisition, HCS was a privately-owned business with limited administrative and accounting resources, accounting software inappropriate for the size of the business and generally weak accounting processes, procedures and controls. Specifically, material weaknesses existed in HCS's processes, procedures and controls with respect to revenue, receivables, payment of payroll taxes and estimating various accrued expenses.

Remediation of Material Weakness

We are working to improve the processes, procedures and controls at HCS and remediate this material weakness. Since the HCS Acquisition in July 2017, we have implemented improvements in processes, procedures and controls and we will continue to do so. We are evaluating the accounting professionals at the Company and HCS and will determine if additional resources with relevant experience are needed. We will disclose in future periods the progress we have made in efforts to remediate this material weakness.

Changes in Internal Control Over Financial Reporting

As a result of the HCS acquisition and the generally weak controls at HCS discussed above, we determined that we have a material weakness in our disclosure controls and procedures. We are working to remediate this material weakness as discussed above, but have not completed the process to document and test the new control processes.

It should be noted that any system of controls, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the system will be met. In designing and operating a control system, one must consider the potential benefits of controls relative to their costs and the reality of limited resources available to allocate to control activities, particularly in smaller companies. In addition, the design of any control system is based in part upon certain assumptions about the likelihood of future events and there can be no assurance that any control will meet its objectives under all potential future conditions. Because of such inherent limitations in any control system, there can be no absolute assurance that control issues, misstatements, and/or fraud will be prevented or detected.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

DIRECTORS AND EXECUTIVE OFFICERS

Howard M. Amster, age 73, has been a member of the Board since 2009. Mr. Amster currently is an owner and operator of multiple real estate investments. Since March 1998, Mr. Amster has served as President of Pleasant Lake Apts. Corp., the corporate general partner of Pleasant Lake Apts. Limited Partnership. In addition, Mr. Amster has served as a director of Phenixfin Corp since August 2020. Mr. Amster served as a director of Maple Leaf Financial, Inc., the holding company for Geauga Savings Bank, until it was acquired by Farmers Banc Corp in 2020. Mr. Amster also served as a Financial Advisor at McDonald Partners, LLC, a securities brokerage firm from 2015 to 2020. From 2000 to 2015, Mr. Amster served as a Principal with Ramat Securities Ltd., a securities brokerage firm. From 1992 to 2000, Mr. Amster was an investment consultant with First Union Securities (formerly EVEREN Securities and formerly Kemper Securities). The Board believes Mr. Amster's qualifications to serve on the Board include his investment experience and his service as a director of public companies.

Howard Timothy Eriksen, age 52, has been a member of the Board since April 2018. Mr. Eriksen has been the Chief Executive Officer and Interim Chief Financial Officer of Solitron Devices, Inc. ("Solitron"), a manufacturer of solid-state semiconductor components, since July 2016. Mr. Eriksen also serves as the Managing Member of Eriksen Capital Management LLC ("ECM"), a Lynden, Washington based investment advisory firm that he founded in 2005. Previously, Mr. Eriksen worked for Walker's Manual, Inc., a publisher of books and newsletters on micro-cap stocks, unlisted stocks and community banks, from 2004 to 2005, and prior to that for Kiewit Pacific Co, a subsidiary of Peter Kiewit Sons, a construction and mining services company, as an administrative engineer on the Benicia Martinez Bridge project. Mr. Eriksen has been a member of the board of directors of Solitron since August 2015. Mr. Eriksen has been a member of the board of directors of TSR Inc. since October 2019, and since December 2019 Lead Independent Director, Chairman of the Audit and Nominating Committees, and a member of the Compensation and Special Committees. Mr. Eriksen received a Bachelor of Arts from The Master's University and a Master of Business Administration from Texas A&M University. The Board believes that Mr. Eriksen's qualifications to serve on the Board include his financial expertise and operating experience at other small-cap companies.

Barry A. Igdaloff, age 66, has been a member of the Board since 2009 and Chairman of the Board since August 2020. Mr. Igdaloff served as the sole proprietor of Rose Capital, a registered investment advisor in Columbus, Ohio, since 1995. Mr. Igdaloff was a director of Dynex Capital, Inc. from 2000 through 2020. Previously, Mr. Igdaloff was a director of Guest Supply, Inc. prior to its acquisition by Sysco Foods in 2001. Prior to entering the investment business, Mr. Igdaloff was an employee of Ernst & Whinney's international tax department. Mr. Igdaloff is a non-practicing CPA and a non-practicing attorney. The Board believes Mr. Igdaloff's qualifications to serve on the Board include his financial expertise, his years of experience as an investment advisor, attorney, and CPA and his service as a director of public companies.

Lee D. Keddie, age 52, has been a member of the Board since April 2018. Mr. Keddie has been President and Chief Executive Officer of CompuMed Inc. (OTC:CMPD) ("CompuMed"), an enterprise telemedicine solutions company, since November 2015. In addition, he has been President and Chief Executive Officer of Value Creation Management Group LLC, a company that invests in and provides consulting to companies that need operational improvement, since September 2014. Previously, Mr. Keddie spent 13 years with HKX, Inc., a developer of control systems for excavators, as a Co-Owner, President & General Manager, from January 1999 to September 2013. Prior to his business leadership roles, Mr. Keddie spent over eight years in both the commercial and military sectors of the aircraft industry. He has been a member of the board of directors of CompuMed since November 2014 and of Stephan Co. (OTC:SPCO), a manufacturer of hair care products, since March 2015. Mr. Keddie was a board member of Essex Rental Corp. (NASDAQ:ESSX), a company that rents and distributes construction lifting equipment, from June 2015 to February 2017. Mr. Keddie is a professional engineer and received an Honors Co-op Mechanical Engineering Degree from the University of Waterloo. He spent two additional years at the University of Toronto in Aerospace Studies. The Board believes Mr. Keddie's qualifications to serve on the Board include his extensive operating expertise and experience as a director of public companies.

David W. Pointer, age 51, has been our Chief Executive Officer since March 27, 2018. He has served as the Managing Partner of V.I. Capital Management, LLC, a registered investment advisory firm that he founded, since January 2008. Prior to that, Mr. Pointer was a Senior Portfolio Manager and Senior Vice President at ICM Asset Management, an employee-owned investment manager, from September 2003 to September 2007, as well as Portfolio Manager at AIM/INVESCO Investments, an investment management firm, from July 1999 to August 2003. Mr. Pointer has served on the Board of Directors of CompuMed, an enterprise telemedicine solutions company, since December 2013 and as Chairman since October 2014, and as Co-Chief Executive Officer from November 2015 to January 2016. He also has served on the Board of Directors of Solitron Devices, Inc., a manufacturer of solid-state semiconductor components since August 2015 and as Chairman since July 2016. Previously, Mr. Pointer served on the Board of Directors of ALCO Stores, Inc., a retailer, from September 2014 to June 2015. Mr. Pointer has taught Corporate Finance as an adjunct faculty in Whitworth University's MBA program as well as Gonzaga University's MBA program and is an expert in financial analysis and financial markets. Mr. Pointer holds a Bachelor of Science in Business Administration from Central Washington University and a Master of Business Administration from the Wharton School of Business at the University of Pennsylvania. Mr. Pointer is a member of the CFA Institute and a Chartered Financial Analyst.

Carolyn K. Campbell, age 50, has served as our Chief Financial Officer since August 2017. She previously worked as an independent contractor in internal audit and tax roles for various businesses from July 2016 to August 2017. From 2007 to March 2016, Ms. Campbell served as the Company's Internal Audit Manager and was responsible for overseeing corporate audit processes and developing and implementing risk-based audit plans and internal controls over financial recordkeeping and reporting. From 2001 to 2004, Ms. Campbell was an internal auditor with Butler Manufacturing Company, a construction engineering company. From 1995 to 2001, Ms. Campbell was employed by Houlihan's Restaurant Group, a developer of restaurant concepts, most recently as a tax analyst. Ms. Campbell holds a Bachelor of Science in Business Administration from the University of Central Missouri.

CORPORATE GOVERNANCE AND RELATED MATTERS

Board Leadership Structure

The Board is led by Mr. Igdaloff, who serves as the Chairman of the Board having such responsibilities set forth in the Company's' Corporate Governance Guidelines. The Board has determined that this leadership structure is in the best interests of the Company's shareholders at this time.

Board and Committee Meetings

During 2020, there were 5 meetings of the Board, 4 meetings of the Audit Committee, 2 meetings of the Compensation Committee and 2 meetings of the Nominating and Corporate Governance Committee, not including actions taken outside of a meeting by unanimous written consent. Each director participated in at least 75% of the meetings of the Board and the committees on which he served during the periods for which he has been a director or committee member. We have no written policy regarding director attendance at our annual meetings of shareholders.

Board Committees

The Board has a standing Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee. The Board has determined that all directors serving on the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are independent with the meaning of SEC and NASDAQ rules. Descriptions of the responsibilities of such committees are provided below. These descriptions are qualified in their entirety by the full text of the written committee charters that may be found on the Company's website at www.novationcompanies.com.

Audit Committee. The responsibilities of the Audit Committee are set forth in its charter and include assisting the Board in fulfilling its oversight responsibility relating to: (i) the integrity of the Company's consolidated financial statements and financial reporting process and its system of internal accounting and financial controls; (ii) the performance of the internal audit function; (iii) the performance of the independent auditors, which would include an evaluation of the independent auditor's qualifications and independence; (iv) the Company's compliance with legal and regulatory requirements, including disclosure controls and procedures; and (v) the preparation of an Audit Committee report to be included in the Company's annual proxy statement. The Audit Committee consists of Barry A. Igdaloff, Howard M. Amster, and Howard Timothy Eriksen, with Mr. Igdaloff serving as the chairman. The Board has determined that Barry A. Igdaloff and Howard Timothy Eriksen qualify as "audit committee financial experts" under SEC rules and that each Audit Committee member has sufficient knowledge in reading and understanding the Company's consolidated financial statements to serve on the Audit Committee.

Nominating and Corporate Governance Committee. The responsibilities of the Nominating and Corporate Governance Committee are set forth in its charter and include the following: (i) identify individuals qualified to become Board members consistent with the criteria established by the Board; (ii) recommend to the Board the director nominees for the next annual meeting of shareholders; (iii) lead the Board in the annual review of the Board's performance and the review of management's performance; and (iv) shape the corporate governance policies and practices including developing a set of corporate governance principles applicable to the Company and recommending them to the Board. The Nominating and Corporate Governance Committee consists of Lee D. Keddie, Howard M. Amster and Barry A. Igdaloff, with Mr. Keddie serving as the chairman.

Compensation Committee. The responsibilities of the Compensation Committee are set forth in its charter and include the following: (i) review and approve the goals, objectives and compensation structure for our Chief Executive Officer, Chief Financial Officer and senior management; (ii) review, approve and recommend to the Board any new incentive-compensation and equity-based plans that are subject to Board approval; and (iii) approve any required disclosure on executive officer compensation for inclusion in the Company's annual proxy statement and Annual Report on Form 10-K. The Compensation Committee consists of Barry A. Igdaloff, Howard M. Amster and Lee D. Keddie, with Mr. Igdaloff serving as the chairman.

Compensation Committee Process and Advisors

The Compensation Committee is responsible for discharging the responsibilities of the Board with respect to the compensation of our executive officers. The Compensation Committee recommends overall compensation of our executive officers to the Board. The Board approves all compensation of our executive officers. The Compensation Committee may form and delegate authority to subcommittees, comprised of one or more members of the Compensation Committee, as necessary or appropriate, and each such subcommittee shall have the full power and authority of the Compensation Committee.

The charter of the Compensation Committee permits the Compensation Committee to engage outside consultants. In 2020, the Compensation Committee did not retain a compensation consultant.

Corporate Governance Documents

The Company's Corporate Governance Guidelines, Code of Conduct, and the charters of the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are available at the Investors-Corporate Governance section of our website, www.novationcompanies.com. The Company will also provide copies of these documents free of charge to any shareholder who sends a written request to: Novation Companies, Inc., Investor Relations, 9229 Ward Parkway, Suite 340, Kansas City, MO 64114.

Code of Ethics

The Company has adopted a Code of Conduct that applies to our directors, principal executive officer, principal financial officer, principal accounting officer, and other employees. The Code of Conduct is available at the Investors-Corporate Governance section of our website, www.novationcompanies.com. We intend to satisfy the disclosure requirements regarding any amendment to, or waiver from, a provision of our Code of Conduct that applies to our principal executive officer, principal financial officer, principal accounting officer, controller or persons performing similar functions by disclosing such matters on our website within four business days.

Our investor relations contact information follows:

Investor Relations
9229 Ward Parkway, Suite 340
Kansas City, Missouri 64114
816.237.7000
Email: ir@novationcompanies.com

Shareholder Communications with the Board

Shareholders may communicate directly with any member of the Board or any individual chairman of a Board committee by writing directly to those individuals at the following address: Novation Companies, Inc., 9229 Ward Parkway, Suite 340, Kansas City, MO 64114. Communications that are intended for the non-management, independent directors generally should be marked to the attention of the chairman of the Nominating and Corporate Governance Committee. The Company's general policy is to forward, and not to intentionally screen, any substantive mail received at the Company's corporate office that is sent directly to a director; however, (i) routine advertisements and business solicitations and (ii) communications deemed to be a security risk or principally for harassment purposes, may not be forwarded in the discretion of the Corporate Secretary, provided that in the latter case the Chairman of the Board is notified thereof.

Risk Oversight

The Board oversees an enterprise-wide approach to risk management, designed to support the achievement of Company objectives, improve long-term Company performance and create shareholder value. A fundamental part of risk management is understanding the risks the Company faces and what steps management is taking to manage those risks, but also understanding what level of risk is appropriate for the Company. The involvement of the full Board in setting the Company's business strategy and objectives is integral to the Board's assessment of the Company's risk and also a determination of what constitutes an appropriate level of risk for the Company. The full Board conducts an annual risk assessment of the Company's financial risk, legal/compliance risk and operational/strategic risk and addresses individual risk issues throughout the year as necessary.

While the Board has the ultimate oversight responsibility for the risk management process, the Board delegates responsibility for certain aspects of risk management to the Audit Committee. Per its charter, the Audit Committee focuses on key financial risks and related controls and processes and discusses with management the Company's major financial reporting exposures and the steps management has taken to monitor and control such exposures.

The Board believes its leadership structure enhances overall risk oversight. While the Board requires risk assessments from management, the combination of Board member experience, diversity of perspectives, continuing education and independence of governance processes provide an effective basis for testing, overseeing and supplementing management assessments.

Identifying and Evaluating Nominees for Directors

The Nominating and Corporate Governance Committee utilizes a variety of methods for identifying and evaluating nominees for director. The Nominating and Corporate Governance Committee regularly assesses the appropriate size of the Board, and whether any vacancies on the Board are expected due to retirement or otherwise. In the event that vacancies are anticipated, or otherwise arise, the Nominating and Corporate Governance Committee considers various potential candidates for director. Candidates may come to the attention of the Nominating and Corporate Governance Committee through current members of the Board, professional search firms, shareholders or other persons. These candidates are evaluated at regular or special meetings of the Nominating and Corporate Governance Committee, and may be considered at any point during the year. Shareholder nominations should be addressed to: Novation Companies, Inc., 9229 Ward Parkway, Suite 340, Kansas City, MO 64114, attention Corporate Secretary. The Nominating and Corporate Governance Committee will consider properly submitted shareholder nominations for candidates for the Board, following verification of the shareholder status of persons proposing candidates. If any materials are provided by a shareholder in connection with the nominating of a director candidate, such material will be forwarded to the Nominating and Corporate Governance Committee. The Nominating and Corporate Governance Committee will also review materials provided by professional search firms or other parties.

The Nominating and Corporate Governance Committee considers candidates for the Board based upon several criteria set forth in the Company's Corporate Governance Guidelines, including their broad-based business and professional skills and experience, education, accounting and financial expertise, age, reputation, civic and community relationships, concern for the long-term interest of shareholders, personal integrity and judgment, knowledge and experience in the Company's industry (such as operations, finance, accounting and marketing experience and education) and diversity. The Nominating and Corporate Governance Committee considers diversity in the broadest sense, thus including factors such as age, gender, race, ethnicity and geographic location, as well as a variety of experience and educational backgrounds when seeking nominees to the Board. The Nominating and Corporate Governance Committee does not have a formal diversity policy in place.

The Nominating and Corporate Governance Committee does not assign specific weights to the criteria and no particular criterion is necessarily applicable to all prospective nominees. When evaluating nominees, the composition of the entire Board is also taken into account, including the need for a majority of independent directors. In addition, the assessment of a candidate includes consideration of the number of public boards on which he or she serves because of the time requirements for duties and responsibilities associated with serving on the Board. The Nominating and Corporate Governance Committee believes that the backgrounds and qualifications of the directors, considered as a group, should provide a significant composite mix of experience, knowledge and abilities that will allow the Board to fulfill its responsibilities. The Nominating and Corporate Governance Committee assesses the effectiveness of the Corporate Governance Guidelines, including with respect to director nominations and qualifications and achievement of having directors with a broad range of experience and backgrounds, through completion of the annual self-evaluation process.

Involvement in Certain Legal Proceedings

V.I. Capital Management, LLC ("V.I. Capital") and Chief Executive Officer David W. Pointer are subject to a consent order (the "Consent Order") from the State of Washington Department of Financial Institutions, Securities Division, dated March 12, 2018 (Order Number S-16-2093-17-CO01), relating to alleged breaches of their fiduciary duty as investment advisors to their clients, including (i) failure to disclose certain conflict of interest stemming from Mr. Pointer's service on the Boards of Directors of CompuMed and Solitron Devices, Inc., (ii) pledging V.I. Capital investment fund assets as collateral for a line of credit for CompuMed, Inc. and failing to disclose such pledge to V.I. Capital's year-end auditor, and (iii) failure to timely distribute audited financial statements and a final fund audit to investors. As conditions of the Consent Order, V.I. Capital and Mr. Pointer agreed to (i) cease and desist from violating the Securities Act of 1933, (ii) pay a fine of $10,000 and (iii) pay costs of $2,500. Mr. Pointer also agreed that he will not be a principal, officer or owner of an investment adviser or broker-dealer for 10 years following the entry of the Consent Order, but he may apply for a securities salesperson or investment adviser representative registration with an acceptable plan of supervision.

Item 11. Executive Compensation

DIRECTOR COMPENSATION

The following table presents a summary of the compensation earned by each director who served on the Board during the fiscal year ended December 31, 2020, other than our Chief Executive Officer Mr. Pointer, whose compensation is described in the Executive Compensation section below:

Name		Fees earned or paid in cash	Stock Awards (1) (2)		Total
Barry A. Igdaloff	$	68,500	—	$	68,500
Howard M. Amster	$	36,000	—	$	36,000
Howard Timothy Eriksen	$	36,000	—	$	36,000
Lee D. Keddie	$	41,000	—	$	41,000

(1) Represents the aggregate grant date fair value computed in accordance with Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 718.
(2) There were no stock awards granted to the Board in 2020.

On September 20, 2019, the Board approved base compensation for each of the Company's non-employee directors, Barry A. Igdaloff, Howard M. Amster, Howard Timothy Eriksen and Lee D. Keddie, in an amount of $36,000 per annum, payable in cash on a quarterly basis and 500,000 shares of restricted stock. The Board approved additional compensation for the chairmen of the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee in the amounts of $15,000, $5,000, and $5,000 per annum, respectively, payable in cash on a quarterly basis. In addition, the Board approved additional compensation for the Lead Independent Director of 100,000 shares of restricted stock. This base compensation was applicable for non-employee directors for the year ended December 31, 2020. On August 13, 2020, the Board appointed Barry A. Igdaloff as Chairman of the Board and approved additional compensation in the amount of $25,000 per annum, payable in cash on a quarterly basis.

In payment of the equity component of the directors' base compensation as discussed above, on October 1, 2019, each of the non-employee directors received 500,000 shares of restricted stock, except Mr. Igdaloff received 600,000 shares, pursuant to the terms and conditions of the 2015 Incentive Plan and each director's respective award agreement. These shares vested at 50% on the first anniversary of the grant date, October 1, 2020, and 50% on the second anniversary of the grant date, October 1, 2021. As stated in the table above, there were no stock awards granted to the Board in 2020.

EXECUTIVE COMPENSATION

Our named executive officers during 2020 (each a "Named Executive Officer") were(i) David W. Pointer, our Chief Executive Officer, and (ii) Carolyn K. Campbell, our Chief Financial Officer.

Summary Compensation Table

The following table sets forth the compensation of our Named Executive Officers for the periods indicated.

Name and Principal Position	Year		Salary		Bonus		Stock Awards (1)		All Other Compensation		Total
David W. Pointer (2) (3) (4)	2020	$	250,000	$	18,000	$	80,000	$	109	$	348,109
Chief Executive Officer	2019	$	131,154	$	150,000	$	100,000	$	90	$	381,244
Carolyn K. Campbell (5) (6) (7)	2020	$	150,000	$	50,000	$	8,250	$	368	$	208,618
Chief Financial Officer	2019	$	150,000	$	46,750	$	12,500	$	340	$	209,590

(1) Represents the aggregate grant date fair value computed in accordance with FASB ASC Topic 718.
(2) Mr. Pointer serves as the Chief Executive Officer of both Novation and HCS.
(3) Represents the grant date fair value of 2,000,000 shares of restricted stock granted to Mr. Pointer on February 4, 2020. 100% of these shares vested on October 1, 2020.
(4) Represents the grant date fair value of 2,000,000 shares of restricted stock granted to Mr. Pointer on January 22, 2019. 100% of these shares vested on October 1, 2019.
(5) Ms. Campbell serves as the Chief Financial Officer of both Novation and HCS.
(6) Represents the grant date fair value of 165,000 shares of restricted stock granted to Ms. Campbell on February 4, 2020. 100% of these shares vested on October 1, 2020.
(7) Represents the grant date fair value of 250,000 shares of restricted stock granted to Ms. Campbell on January 22, 2019. 100% of these shares vested on October 1, 2019.

Outstanding Equity Awards at Fiscal Year-End 2020

There were no outstanding equity incentive plan awards for our Named Executive Officers as of December 31, 2020.

Employment Agreements and Arrangements with Named Executive Officers

David W. Pointer

Mr. Pointer entered an employment agreement with the Company on October 1, 2019 (the "Pointer Employment Agreement"). Mr. Pointer's base salary is $250,000, and he is eligible to earn an annual bonus, based on performance benchmarks, and to participate in any equity programs of the Company, at the Company's discretion. The Pointer Employment Agreement has an indefinite term and provided that Mr. Pointer is an employee "at-will," and his employment may be terminated at any time by either party, with or without cause, for any reason or no reason. If Mr. Pointer's employment is terminated by the Company other than for "cause" or by Mr. Pointer for "good reason" (each as defined in the Pointer Employment Agreement), Mr. Pointer will receive, over a period of 6 months following termination, compensation at an annual rate equal to his then-existing annual base salary.

Carolyn K. Campbell

Ms. Campbell entered an employment agreement with the Company on August 9, 2017 (the "Campbell Employment Agreement"). Ms. Campbell's base salary is $150,000, and she is eligible to participate in any equity programs of the Company, at the Company's' discretion. The Campbell Employment Agreement has an indefinite term and provided that Ms. Campbell is an employee "at-will," and her employment may be terminated at any time by either party, with or without cause, for any reason or no reason. If Ms. Campbell's employment is terminated by the Company other than for "cause" or by Ms. Campbell for "good reason" (each as defined in the Campbell Employment Agreement), Ms. Campbell will receive, over a period of 3 months following termination, compensation at an annual rate equal to her then-existing annual base salary.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

The following table sets forth sets forth certain information with respect to beneficial ownership of the Company's common stock as of March 4, 2021 by: (i) each person, or group of affiliated persons, known to us to beneficially own more than 5% of our outstanding common stock, (ii) each of our directors and named executive officers, and (iii) all of our current directors and executive officers as a group. The amounts and percentages of common stock beneficially owned are reported on the basis of regulations of the SEC governing the determination of beneficial ownership of securities. The information relating to 5% beneficial owners is based on information we received from such holders. Except as otherwise set forth below, the address of the persons listed below is c/o Novation Companies, Inc., 9229 Ward Parkway, Suite 340, Kansas City, MO 64114.

	Beneficial Ownership of Common Stock	
Name of Beneficial Owner	Shares	Percent of Class (1)
Directors and Named Executive Officers		
Howard M. Amster (2)	500,000	*
Howard Timothy Eriksen (3)	1,333,333	1.1%
Barry A. Igdaloff (4)	6,953,390	6.2%
Lee D. Keddie (5)	1,333,333	1.1%
Carolyn K. Campbell (6)	565,000	*
David W. Pointer (7)	5,000,000	4.3%
All current directors and executive officers as a group (6 persons) (8)	15,685,056	13.7%
5% Beneficial Owners		
Massachusetts Mutual Life Insurance Company (9)	19,258,775	16.5%

* Less than 1%

(1) Based on 116,655,893 shares of common stock outstanding as of February 25, 2021. Shares of common stock issuable upon exercise of options, warrants or other rights or the conversion of other convertible securities beneficially owned that are exercisable or convertible within 60 days are deemed outstanding for the purpose of computing the percentage ownership of the person holding such securities and rights and all directors and executive officers as a group.

(2) Consists of 250,000 shares of common stock, 250,000 shares of unvested restricted stock.

(3) Consists of 1,083,333 shares of common stock and 250,000 shares unvested restricted stock.

(4) Consists of 3,529,707 shares of common stock, 300,000 shares of unvested restricted stock and 3,123,683 shares of common stock controlled by Mr. Igdaloff as a registered investment advisor.

(5) Consists of 1,083,333 shares of common stock and 250,000 shares unvested restricted stock.

(6) Consists of 565,000 shares of common stock.

(7) Consists of 3,000,000 shares of common stock and 2,000,000 shares of unvested restricted stock.

(8) Consists of 9,511,373 shares of common stock; 3,050,000 shares of unvested restricted stock.

(9) Based on a Form 3 filed on December 14, 2011, Massachusetts Mutual Life Insurance Company ("MassMutual") may be deemed to own beneficially and indirectly 19,258,775 shares of common stock held in one or more advisory accounts and private investment funds. Babson Capital Management LLC acts as investment adviser to these advisory accounts and private investment funds, and in such capacities may also be deemed to be the beneficial owner of such shares. The address of MassMutual is 1295 State Street, Springfield, MA 01111.

Equity Compensation Plan Information

The following table sets forth information as of December 31, 2020 with respect to compensation plans under which the Company's common stock may be issued.

Plan Category	Number of Securities to be Issued Upon Exercise of Outstanding Options, Warrants and Rights	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Shares Reflected in the First Column)
Equity compensation plans approved by stockholders (1)	—	—	3,974,211
Equity compensation plans not approved by stockholder	—	—	—
Total	—	—	3,974,211

(1) Represents shares that may be issued pursuant to outstanding options awarded under the 2015 Incentive Plan.

Item 13. Certain Relationships and Related Transactions, and Director Independence

Related Party Transactions

The Company has adopted a written policy that addresses the review, approval or ratification of any transaction, arrangement, or relationship or series of similar transactions, arrangements or relationships, including any indebtedness or guarantee of indebtedness, between the Company and any related party, in which the aggregate amount involved exceeds the lesser of $120,000 or 1% of the average of the Company's total assets at year-end for the last two completed fiscal years. Under the policy, a related party of the Company includes:

- Any executive officer, or any director or nominee for election as a director;
- Any person who owns more than 5% of the Company's voting securities;
- Any immediate family member of any of the foregoing; or
- Any entity in which any of the foregoing persons is employed or is a partner or principal or in a similar position or in which such person has a 10% beneficial ownership interest.

Under the policy, the Board reviews the material facts of any related party transaction and approves it prior to its occurrence. If advance approval is not feasible, then the Board will either ratify the transaction at its next regularly scheduled meeting or the transaction will be rescinded. In making its determination to approve or ratify any related party transaction, the Board may consider such factors as (i) the extent of the related party's interest in the transaction, (ii) if applicable, the availability of other sources of comparable products or services, (iii) whether the terms of the transaction are no less favorable than terms generally available to Company in unaffiliated transactions under like circumstances, (iv) the benefit to the Company, and (v) the aggregate value of the transaction.

No director may engage in any Board discussion or approval of any related party transaction in which he or she is a related party, but that director is required to provide the Board with all material information reasonably requested concerning the transaction.

Director Independence

The Board has determined that all of our non-employee directors are independent within the meaning of SEC and NASDAQ rules. The Board has also determined that all directors serving on the Audit Committee, Compensation Committee and Nominating and Corporate Governance Committee are independent within the meaning of SEC and NASDAQ rules. Although the Company's securities are not listed on NASDAQ, the Company uses the independence standards provided in NASDAQ rules in determining whether or not our directors are independent.

Item 14. Principal Accountant Fees and Services

Audit Fees

The following table presents aggregate fees billed for professional services rendered by Boulay PLLP. There were no other professional services rendered or fees billed by Boulay PLLP.

	For the Fiscal Years Ended December 31,	
	2020	2019
Audit Fees (1)	$ 95,400	$ 122,000
Tax Fees (2)	7,020	11,000
Total Fees	$ 102,420	$ 133,000

(1) Annual audit and quarterly reviews of our consolidated financial statements, assistance with and review of documents filed with the SEC.
(2) Preparation and filing of annual state and federal income taxes.

Pre-Approval Policies and Procedures

The Audit Committee has adopted a policy with respect to the pre-approval of all audit and non-audit services provided by our independent registered public accounting firm. All fees paid to our independent registered public accounting firm for fiscal years 2020 and 2019 were pre-approved in accordance with these policies. Generally, the policy requires that the Audit Committee annually approve fees exceeding $50,000 for audit services, audit-related and tax services. Fees expected to exceed $10,000 for all other services must be approved prior to engagement for those services.

PART IV

Item 15. Exhibits and Financial Statements Schedules

Financial Statements and Schedules

(1) The financial statements as set forth under Item 8 of this Form 10-K are included herein.
(2) The required financial statement schedules are omitted because the information is disclosed elsewhere herein.

Exhibits

We describe the exhibits filed as part of, or incorporated by reference into, this Form 10-K in the Exhibit Index below.

Item 16. Form 10-K Summary

None.

EXHIBIT INDEX

Exhibit No.	Description of Document
2.1	Membership Interest Purchase Agreement, dated as of December 21, 2015, by and among Novation Companies, Inc., Corvisa Services LLC and ShoreTel, Inc. (incorporated by reference to Exhibit 2.1 to the Current Report on Form 8-K filed on December 21, 2015).
2.2	Stock Purchase Agreement, dated as of February 1, 2017, by and among Novation Companies, Inc., Novation Holding, Inc., Healthcare Staffing, Inc. and Butler America, LLC (incorporated by reference to Exhibit 2.1 on the Current Report on Form 8-K filed on February 3, 2017).**
2.3	Closing Agreement, dated as of July 27, 2017, by and among Novation Companies, Inc., Novation Holding, Inc., Healthcare Staffing, Inc. and Butler America, LLC (incorporated by reference to Exhibit 2.1 on the Quarterly Report on Form 10-Q filed on February 26, 2018).
3.1	Articles of Amendment and Restatement (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on August 2, 2017).
3.2	Articles of Amendment to Articles of Amendment and Restatement (incorporated by reference to Exhibit 3.1 to the Current Report on Form 8-K filed on December 14, 2018).
3.3	Second Amended and Restated Bylaws (incorporated by reference to Exhibit 3.2 to the Current Report on Form 8-K filed on August 2, 2017).
4.1	Specimen Common Stock Certificate (incorporated by reference to Exhibit 4.1 to the Quarterly Report Form 10-Q filed on August 5, 2005).
4.2	Rights Agreement, dated as of September 15, 2011, by and between NovaStar Financial, Inc. and Computershare Trust Company, N.A., as rights agent (incorporated by reference to Exhibit 4.1 to the Current Report on Form 8-K filed on September 21, 2011).
4.3	First Amendment to Rights Agreement, dated June 20, 2014, by and between the Company and Computershare Trust Company, N.A. (incorporated by reference to Exhibit 4.2 to Form 8-A/A filed on June 20, 2014).
4.4	Second Amendment to Rights Agreement, dated August 24, 2015, by and between the Company and Computershare Trust Company, N.A. (incorporated by reference to Exhibit 4.3 to the Form 8-A12G filed on August 28, 2015).
4.5	Third Amendment to Rights Agreement, dated as of July 20, 2018, between Novation Companies, Inc. and Computershare Trust Company, N.A. (incorporated by reference to Exhibit 4.1 on the Current Report on Form 8-K filed on July 25, 2018).
4.6	Description of the Company's Securities (incorporated by reference to Exhibit 4.6 to the Annual Report on Form 10-K filed on March 23, 2020).
10.1	Novation Companies, Inc. Amended 2015 Incentive Stock Plan (incorporated by reference to Exhibit 4.1 to the Registration Statement on Form S-8 filed on September 21, 2020).*
10.2	Form of Restricted Stock Award Agreement for Non-Employee Directors under the Novation Companies, Inc. 2015 Incentive Stock Plan (incorporated by reference to Exhibit 10.3 to the Annual Report on Form 10-K filed on October 26, 2017).*
10.3	Form of Restricted Stock Award Agreement for Employees under the Novation Companies, Inc. 2015 Incentive Stock Plan (incorporated by reference to Exhibit 10.4 to the Annual Report on Form 10-K filed on October 26, 2017).*
10.4	Amended and Restated 2004 Incentive Stock Plan (as amended May 29, 2014) (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed on May 30, 2014).*
10.5	First Amendment to the Company's Amended and Restated 2004 Incentive Stock Plan (incorporated by reference to Appendix A to Form DEF 14A filed on April 25, 2014).*
10.6	Form of Stock Option Agreement under NovaStar Financial, Inc. 2004 Incentive Stock Plan (incorporated by reference to Exhibit 10.25.1 to the Current Report on Form 8-K filed on February 4, 2005).*
10.7	Form of Restricted Stock Award Agreement under NovaStar Financial, Inc. 2004 Incentive Stock Plan (incorporated by reference to Exhibit 10.25.2 to the Current Report on Form 8-K filed on February 4, 2005).*
10.8	Form of Employee Non-Qualified Stock Option Agreement under the Company's Amended and Restated 2004 Incentive Stock Plan (incorporated by reference to Exhibit 10.4 to the Annual Report on Form 10-Q filed on August 7, 2014).*
10.9	Employment Agreement, dated as of October 1, 2019, by and between Novation Companies, Inc. and David W. Pointer (incorporated by reference to Exhibit 10.1 to the Current Report on Form 8-K filed on September 25, 2019).*

10.10	Employment Agreement, dated as of August 9, 2017, by and between Novation Companies, Inc. and Carolyn Campbell (incorporated by reference to Exhibit 10.11 to the Annual Report on Form 10-K filed on April 10, 2018).*
10.11	Senior Secured Note Purchase Agreement, dated as of July 27, 2017, among Novation Companies, Inc., Novation Holding, Inc., Healthcare Staffing, Inc., Taberna Preferred Funding I, Ltd., Taberna Preferred Funding II, Ltd., Kodiak CDO I, Ltd., and Wilmington Savings Fund Society, FSB (incorporated by reference to Exhibit 10.1 on the Quarterly Report on Form 10-Q filed on February 26, 2018).
10.12	First Amendment to Senior Secured Note Purchase Agreement (incorporated by reference to Exhibit 10.1 on the Quarterly Report on Form 10-Q filed on August 12, 2019).
21.1	Subsidiaries of the Registrant.
23.1	Consent of Boulay PLLP.
31.1	Principal Executive Officer Certification filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Principal Financial Officer Certification filed pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Principal Executive Officer Certification furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Principal Financial Officer Certification furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	The following financial information from Novation Companies, Inc.'s Annual Report on Form 10-K for the year ended December 31, 2020, formatted in XBRL (Extensible Business Reporting Language) includes: (i) Consolidated Balance Sheets as of December 31, 2020 and December 31, 2019, (ii) Consolidated Statements of Operations for the years ended December 31, 2020 and 2019, (iii) Consolidated Statements of Comprehensive Income for the years ended December 31, 2020 and 2019, (iv) Consolidated Statements of Shareholders' Deficit for the years ended December 31, 2020 and 2019, (v) Consolidated Statements of Cash Flows for the years ended December 31, 2020 and 2019, and (vi) the Notes to Consolidated Financial Statements.

* Management contract or compensatory plan or arrangement.

** The registrant has omitted certain schedules and exhibits to this agreement in accordance with Item 601(b)(2) of Regulation S-K, and will supplementally furnish a copy of any omitted schedule and/or exhibit to the Securities and Exchange Commission upon request.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

NOVATION COMPANIES, INC.

DATE: March 4, 2021	/s/ DAVID W. POINTER David W. Pointer, Chief Executive Officer
DATE: March 4, 2021	/s/ CAROLYN K. CAMPBELL Carolyn K. Campbell, Chief Financial Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and dates indicated.

DATE: March 4, 2021	/s/ DAVID W. POINTER David W. Pointer, Chief Executive Officer (Principal Executive Officer)
DATE: March 4, 2021	/s/ CAROLYN K. CAMPBELL Carolyn K. Campbell, Chief Financial Officer (Principal Financial Officer and Principal Accounting Officer)
DATE: March 4, 2021	/s/ HOWARD M. AMSTER Howard M. Amster, Director
DATE: March 4, 2021	/s/ HOWARD TIMOTHY ERIKSEN Howard T. Eriksen, Director
DATE: March 4, 2021	/s/ BARRY A. IGDALOFF Barry A. Igdaloff, Director and Chairman
DATE: March 4, 2021	/s/ LEE D. KEDDIE Lee D. Keddie, Director

Exhibit 21.1

SUBSIDIARIES OF THE REGISTRANT

Novation Holding, Inc., a Delaware Corporation
Healthcare Staffing, Inc., a Georgia corporation
NovaStar Mortgage LLC, a Virginia limited liability company
NovaStar Mortgage Funding Corporation, a Delaware corporation
NovaStar REMIC Financing Corporation, a Delaware corporation

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements on Form S-8 (File No. 333-248947, File 333-206184, File No. 333-196909, and File No. 333-116998) of Novation Companies, Inc. of our report dated March 4, 2021 relating to the consolidated financial statements that appear in this Annual Report on Form 10-K as of and for the year ended December 31, 2020. Our report dated March 4, 2021 contained an emphasis of matter paragraph related to substantial doubt about the Company to continue as a going concern.

/s/ BOULAY PLLP

Minneapolis, MN
March 4, 2021

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, David W. Pointer, certify that:

1. I have reviewed this Annual Report on Form 10-K of Novation Companies, 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 registrant's board of directors (or persons performing the equivalent function):

    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 controls over financial reporting.

DATE: March 4, 2021

/s/ David W. Pointer
David W. Pointer
Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

I, Carolyn K. Campbell, certify that:

1. I have reviewed this Annual Report on Form 10-K of Novation Companies, 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 registrant's board of directors (or persons performing the equivalent function):

   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 controls over financial reporting.

DATE: March 4, 2021

/s/ Carolyn K. Campbell
Carolyn K. Campbell
Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Novation Companies, Inc. (the "Company") on Form 10-K for the period ended December 31, 2020, as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, David W. Pointer, Chief Executive Officer of the Company, certify as of the date hereof, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes - Oxley Act of 2002, that to my 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.

DATE: March 4, 2021

/s/ David W. Pointer
David W. Pointer
Chief Executive Officer
(Principal Executive Officer)

Exhibit 32.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

In connection with the Annual Report of Novation Companies, Inc. (the “Company”) on Form 10-K for the period ended December 31, 2020, as filed with the Securities and Exchange Commission on the date hereof (the “Report”), I, Carolyn K. Campbell, Chief Financial Officer of the Company, certify as of the date hereof, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes - Oxley Act of 2002, that to my 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.

DATE: March 4, 2021

/s/ Carolyn K. Campbell
Carolyn K. Campbell
Chief Financial Officer
(Principal Financial Officer)