

Report of Organizational Actions Affecting Basis of Securities

▶ See separate instructions.

Part I Reporting Issuer

1 Issuer's name NOVAN, INC.		2 Issuer's employer identification number (EIN) 20-4427682	
3 Name of contact for additional information RICHARD PETERSON		4 Telephone No. of contact 919-485-8080	
6 Number and street (or P.O. box if mail is not delivered to street address) of contact 4105 HOPSON ROAD		5 Email address of contact RPETERSON@NOVAN.COM	
8 Date of action SEPTEMBER 26, 2016		7 City, town, or post office, state, and Zip code of contact MORRISVILLE, NC 27560	
9 Classification and description CONVERSION OF PREFERRED STOCK TO COMMON STOCK			
10 CUSIP number 66988N109	11 Serial number(s) N/A	12 Ticker symbol NASDAQ: NOVN	13 Account number(s) N/A

Part II Organizational Action Attach additional statements if needed. See back of form for additional questions.

14 Describe the organizational action and, if applicable, the date of the action or the date against which shareholders' ownership is measured for the action ▶ **ON SEPTEMBER 26, 2016, IMMEDIATELY PRIOR TO THE CLOSING OF NOVAN, INC.'S (THE "COMPANY") INITIAL PUBLIC OFFERING, ALL OF THE SHARES OF THE COMPANY'S CONVERTIBLE PREFERRED STOCK THEN OUTSTANDING WERE CONVERTED INTO 8,776,269 SHARES OF COMMON STOCK (THE "IPO CONVERSION"). NO FRACTIONAL SHARES OF COMMON STOCK WERE ISSUED IN CONNECTION WITH THE IPO CONVERSION. INSTEAD, SHAREHOLDERS OF OUTSTANDING PREFERRED STOCK WHO WOULD OTHERWISE BE ENTITLED TO RECEIVE A FRACTION SHARE OF COMMON STOCK AS A RESULT OF THE IPO CONVERSION WERE ENTITLED TO RECEIVE CASH IN LIEU THEREOF.**

15 Describe the quantitative effect of the organizational action on the basis of the security in the hands of a U.S. taxpayer as an adjustment per share or as a percentage of old basis ▶ **THE AGGREGATE TAX BASIS IN THE SHARES RECEIVED IN THE IPO CONVERSION, INCLUDING ANY FRACTIONAL SHARES TREATED AS RECEIVED AND THEN EXCHANGED FOR CASH, SHOULD BE EQUAL TO THE TOTAL TAX BASIS IN THE SHARES EXCHANGED, AND THE HOLDING PERIOD OF THE SHARES RECEIVED IN THE IPO CONVERSION WILL INCLUDE THE HOLDING PERIOD OF THE SHARES EXCHANGED. A SHAREHOLDER'S TAX BASIS IN SHARES OF COMMON STOCK AFTER THE IPO CONVERSION SHOULD EQUAL THE SHAREHOLDER'S TAX BASIS IN THE SHARES OF CONVERTIBLE PREFERRED STOCK EXCHANGED. A SHAREHOLDER'S TOTAL TAX BASIS IN SUCH COMMON STOCK RECEIVED IN THE IPO CONVERSION IMMEDIATELY AFTER THE DEEMED SALE OF FRACTIONAL SHARES SHOULD EQUAL THAT SHAREHOLDER'S TOTAL TAX BASIS IN THAT SHAREHOLDER'S PRE-IPO CONVERSION CONVERTIBLE PREFERRED SHARES, LESS THE TAX BASIS ALLOCATED TO THE FRACTIONAL SHARES RECEIVED.**

16 Describe the calculation of the change in basis and the data that supports the calculation, such as the market values of securities and the valuation dates ▶ **AS DISCUSSED IN ITEM 15 ABOVE, THE AGGREGATE TAX BASIS IN THE COMMON STOCK RECEIVED IN THE IPO CONVERSION, INCLUDING ANY FRACTIONAL SHARES TREATED AS RECEIVED AND THEN EXCHANGED FOR CASH, SHOULD BE EQUAL TO THE TOTAL TAX BASIS IN THE SHARES OF CONVERTIBLE PREFERRED STOCK EXCHANGED. THE MARKET VALUE OF THE COMMON STOCK WAS NOT APPLICABLE IN DETERMINING A SHAREHOLDER'S TAX BASIS IN THE COMMON STOCK RECEIVED IN THE IPO CONVERSION.**

Part II Organizational Action (continued)

17 List the applicable Internal Revenue Code section(s) and subsection(s) upon which the tax treatment is based ► **SECTION 302 SECTION 1001, SECTION 1031, SECTION 1036, SECTION 1221 AND SECTION 1222. EACH SHAREHOLDER SHOULD CONSULT HIS OR HER OWN TAX ADVISOR WITH RESPECT TO THE QUANTITATIVE EFFECT OF THE IPO CONVERSION ON THE TAX BASIS OF SUCH SHAREHOLDER'S COMMON STOCK RECEIVED IN THE IPO CONVERSION.**

18 Can any resulting loss be recognized? ► **EXCEPT TO THE EXTENT OF CASH RECEIVED, IF ANY, IN LIEU OF FRACTIONAL SHARES, A SHAREHOLDER SHOULD NOT RECOGNIZE GAIN OR LOSS IN CONNECTION WITH THE IPO CONVERSION. SHAREHOLDERS ENTITLED TO FRACTIONAL SHARES IN THE IPO CONVERSION ARE DEEMED TO HAVE RECEIVED AND THEN IMMEDIATELY SOLD SUCH FRACTIONAL SHARES FOR CASH. IN GENERAL, IF A SHAREHOLDER RECEIVES CASH IN LIEU OF A FRACTIONAL SHARE, THE SHAREHOLDER SHOULD RECOGNIZE GAIN OR LOSS, SUBJECT TO THE RELEVANT LOSS LIMITATION PROVISIONS OF THE INTERNAL REVENUE CODE, BASED ON THE DIFFERENCE BETWEEN THE CASH RECEIVED AND THE ADJUSTED TAX BASIS IN THE FRACTIONAL SHARE. EACH SHAREHOLDER IS ADVISED TO CONSULT HIS OR HER OWN TAX ADVISOR AS TO THE GAIN OR LOSS RECOGNIZED IN CONNECTION WITH THE DEEMED SALE OF FRACTIONAL SHARES IN THE IPO CONVERSION.**

19 Provide any other information necessary to implement the adjustment, such as the reportable tax year ► **THE COMPANY COMPLETED THE IPO CONVERSION ON SEPTEMBER 26, 2016, SUCH THAT THE ORGANIZATIONAL ACTION OCCURRED DURING THE COMPANY'S TAXABLE PERIOD ENDING DECEMBER 31, 2016. THE REPORTABLE TAX YEAR IS 2016 FOR CALENDAR YEAR TAXPAYERS. FOR SHAREHOLDERS REPORTING TAXABLE INCOME ON A BASIS OTHER THAN THE CALENDAR YEAR, THE REPORTABLE TAX YEAR OF THE IPO CONVERSION IS THE SHAREHOLDER'S TAX YEAR THAT INCLUDES SEPTEMBER 26, 2016.**

Under penalties of perjury, I declare that I have examined this return, including accompanying schedules and statements, and to the best of my knowledge and belief, it is true, correct, and complete. Declaration of preparer (other than officer) is based on all information of which preparer has any knowledge.

Sign Here

Signature ►  Date ► 10/20/2016

Print your name ► **RICHARD PETERSON** Title ► **CHIEF FINANCIAL OFFICER**

Paid Preparer Use Only

Print/Type preparer's name	Preparer's signature	Date	Check <input type="checkbox"/> if self-employed	PTIN
Firm's name ►			Firm's EIN ►	
Firm's address ►			Phone no.	