

21ST CENTURY HOLDING CO
Form 10-Q
August 09, 2007

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED June 30, 2007
OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____

Commission File number 0-2500111

21st Century Holding Company

(Exact name of registrant as specified in its charter)

Florida

(State or Other Jurisdiction of
Incorporation or Organization)

65-0248866

(IRS Employer
Identification Number)

3661 West Oakland Park Boulevard, Suite 300, Lauderdale Lakes, Florida 33311

(Address of principal executive offices) (Zip Code)

954-581-9993

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such 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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$.01 par value - 8,023,944 outstanding as of August 08, 2007

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21ST CENTURY HOLDING COMPANY**INDEX**

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PART I: FINANCIAL INFORMATION**Item 1**21st CENTURY HOLDING COMPANY
CONSOLIDATED BALANCE SHEETS

| ASSETS | Period Ending | |
|---|------------------------|-------------------|
| | June 30, 2007 | December 31, 2006 |
| | (Dollars in Thousands) | |
| Investments | | |
| Fixed maturities, available for sale, at fair value | \$ 131,441 | \$ 98,525 |
| Fixed maturities, held to maturity, at amortized cost | 20,373 | 19,667 |
| Equity securities, available for sale, at fair value | 4,250 | 6,641 |
| Total investments | 156,064 | 124,834 |
| Cash and short term investments | 7,680 | 17,917 |
| Receivable for investments sold | 5,000 | - |
| Finance contracts, net of allowance for credit losses of \$97 in 2007 and \$116 in 2006, and net of unearned finance charges of \$76 in 2007 and \$90 in 2006 | 1,484 | 1,831 |
| Prepaid reinsurance premiums | 21,366 | 38,927 |
| Premiums receivable, net of allowance for credit losses of \$464 and \$66, respectively | 7,047 | 7,222 |
| Reinsurance recoverable, net | 3,047 | - |
| Deferred policy acquisition costs | 12,470 | 11,153 |
| Deferred income taxes, net | 6,128 | 3,610 |
| Income taxes receivable | 1,104 | 787 |
| Property, plant and equipment, net | 1,171 | 1,296 |
| Other assets | 10,710 | 4,556 |
| Total assets | \$ 233,271 | \$ 212,134 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Unpaid losses and LAE | \$ 45,206 | \$ 39,615 |
| Unearned premiums | 90,668 | 77,829 |
| Due to reinsurers, net | - | 4,237 |
| Premiums deposits and customer credit balances | 4,169 | 3,793 |
| Revolving credit outstanding | 10 | 10 |
| Bank overdraft | 10,573 | 8,107 |
| Subordinated debt | 2,083 | 4,167 |
| Deferred gain from sale of property | 2,233 | 2,467 |
| Accounts payable and accrued expenses | 3,397 | 5,715 |
| Total liabilities | 158,340 | 145,940 |

Commitments and Contingencies

Shareholders' equity:

Common stock, \$0.01 par value. Authorized 37,500,000 shares; issued and outstanding

| | | |
|--|---------------|---------------|
| 7,885,383 and 7,896,919, respectively | 79 | 79 |
| Additional paid-in capital | 48,036 | 47,070 |
| Accumulated other comprehensive income (deficit) | (1,640) | (967) |
| Retained earnings | 28,456 | 20,011 |
| Total shareholders' equity | 74,931 | 66,193 |
| Total liabilities and shareholders' equity | \$ 233,271 | \$ 212,134 |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

21ST CENTURY HOLDING COMPANY
CONSOLIDATED STATEMENTS OF OPERATIONS
(UNAUDITED)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--|-----------|--|-----------|
| | 2007 | 2006 | 2007 | 2006 |
| | (Dollars in Thousands except EPS and dividend data) | | (Dollars in Thousands except EPS and dividend data) | |
| Revenue: | | | | |
| Gross premiums written | \$ 44,462 | \$ 50,753 | \$ 93,652 | \$ 86,362 |
| Gross premiums ceded | (15,803) | (3,372) | (15,809) | (3,372) |
| Net premiums written | 28,658 | 47,381 | 77,843 | 82,990 |
| (Decrease) in prepaid reinsurance premiums | (846) | (593) | (17,818) | (9,265) |
| (Increase) in unearned premiums | (2,999) | (18,047) | (12,839) | (23,177) |
| Net change in prepaid reinsurance premiums and unearned premiums | (3,845) | (18,640) | (30,657) | (32,442) |
| Net premiums earned | 24,814 | 28,741 | 47,187 | 50,548 |
| Commission income | 6,491 | 132 | 6,491 | 159 |
| Finance revenue | 160 | 496 | 347 | 1,132 |
| Managing general agent fees | 804 | 723 | 1,422 | 1,381 |
| Net investment income | 2,131 | 1,612 | 3,700 | 2,808 |
| Net realized investment gains (losses) | 80 | 283 | (48) | 480 |
| Other income | 13 | 355 | 979 | 949 |
| Total revenue | 34,493 | 32,342 | 60,078 | 57,457 |
| Expenses: | | | | |
| Loss and LAE | 9,658 | 9,343 | 23,760 | 16,912 |
| Operating and underwriting expenses | 3,100 | 2,308 | 7,065 | 4,613 |
| Salaries and wages | 1,734 | 1,773 | 3,290 | 3,610 |
| Interest expense | 60 | 181 | 145 | 410 |
| Policy acquisition costs, net of amortization | 4,909 | 4,127 | 9,517 | 8,045 |
| Total expenses | 19,460 | 17,732 | 43,777 | 33,590 |
| Income before provision for income tax expense | 15,033 | 14,610 | 16,300 | 23,866 |
| Provision for income tax expense | 4,555 | 5,705 | 4,979 | 8,949 |
| Net income | \$ 10,478 | \$ 8,905 | \$ 11,321 | \$ 14,918 |

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| | | | | | | | | |
|--|----|-----------|----|-----------|----|-----------|----|-----------|
| Basic net income per share | \$ | 1.32 | \$ | 1.20 | \$ | 1.42 | \$ | 2.02 |
| Fully diluted net income per share | \$ | 1.31 | \$ | 1.19 | \$ | 1.40 | \$ | 1.89 |
| Weighted average number of common shares outstanding | | 7,930,964 | | 7,427,765 | | 7,944,933 | | 7,370,592 |
| Weighted average number of common shares outstanding (assuming dilution) | | 8,014,947 | | 7,465,896 | | 8,099,187 | | 7,880,251 |
| Dividends paid per share | \$ | 0.18 | \$ | 0.12 | \$ | 0.36 | \$ | 0.24 |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

21ST CENTURY HOLDING COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

Six Months Ended June 30,
2007 2006

(Dollars in Thousands)

Cash flow from operating activities:

| | | | | |
|---|----|-----------|----|-----------|
| Net income | \$ | 11,321 | \$ | 14,918 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | | | |
| Amortization of investment discount, net | | (180) | | (143) |
| Depreciation and amortization of property plant and equipment, net | | 155 | | 170 |
| Net realized investment (losses) gains | | (48) | | 480 |
| Common Stock issued for interest on Notes | | 109 | | 128 |
| (Recovery) provision for credit losses, net | | (6) | | 95 |
| Provision (recovery)for uncollectible premiums receivable | | 397 | | (0) |
| Non-cash compensation | | 143 | | 280 |
| Changes in operating assets and liabilities: | | | | |
| Premiums receivable | | (222) | | (2,726) |
| Prepaid reinsurance premiums | | 17,561 | | 9,265 |
| Reinsurance recoverable, net | | (7,284) | | 120,508 |
| Income taxes recoverable | | (316) | | - |
| Deferred income tax expense | | (2,518) | | (2,292) |
| Policy acquisition costs, net of amortization | | (1,317) | | (2,761) |
| Premium finance contracts receivable | | 354 | | 3,494 |
| Other assets | | (6,392) | | 1,890 |
| Unpaid losses and LAE | | 5,591 | | (122,694) |
| Unearned premiums | | 12,839 | | 23,177 |
| Premium deposits and customer credit balances | | 376 | | 1,258 |
| Funds held under reinsurance treaties | | - | | 24 |
| Income taxes payable | | - | | 4,698 |
| Bank overdraft | | 2,466 | | (1,946) |
| Accounts payable and accrued expenses | | (2,318) | | 1,487 |
| Net cash provided by operating activities | | 30,711 | | 49,312 |
| Cash flow used in investing activities: | | | | |
| Proceeds from sale of investment securities available for sale | | 72,033 | | 175,207 |
| Purchases of investment securities available for sale | | (108,708) | | (226,456) |
| Purchases of property and equipment | | (30) | | (353) |
| Proceeds from sale of assets | | - | | 2,663 |
| Net cash used in investing activities | | (36,705) | | (48,939) |
| Cash flow (used in) provided by financing activities: | | | | |
| Subordinated debt | | - | | (1,667) |
| Exercised stock options | | 89 | | 1,417 |
| Dividends paid | | (2,876) | | (1,856) |
| Exercised warrants, net | | - | | 6,061 |
| Purchase of treasury stock | | (1,518) | | (2,001) |
| Tax benefit related to non-cash compensation | | 63 | | 1,758 |
| Revolving credit outstanding | | 0 | | (197) |

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| | | |
|--|----------|----------|
| Net cash (used in) provided by financing activities | (4,242) | 3,515 |
| Net (decrease) increase in cash and short term investments | (10,236) | 3,888 |
| Cash and short term investments at beginning of period | 17,917 | 6,071 |
| Cash and short term investments at end of period | \$ 7,680 | \$ 9,959 |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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21ST CENTURY HOLDING COMPANY
CONSOLIDATED STATEMENTS OF CASH FLOWS
(UNAUDITED)

| (continued) | 2007 | 2006 |
|--|----------|----------|
| Supplemental disclosure of cash flow information: | | |
| Cash paid during the period for: | | |
| Interest | \$ 2 | \$ 160 |
| Income taxes | \$ 7,300 | \$ 4,650 |
| Non-cash investing and finance activities: | | |
| Accrued dividends payable | \$ 1,444 | \$ 972 |
| Retirement of subordinated debt by common stock issuance | \$ 2,083 | \$ 1,667 |
| Stock issued to pay interest on subordinated debt | \$ 109 | \$ 128 |

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

21st Century Holding Company
Notes to Consolidated Financial Statements

(1) Organization and Business

The accompanying unaudited consolidated financial statements of 21st Century Holding Company have been prepared in accordance with generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions for Form 10-Q and Rule 10-01 of Regulation S-X. These financial statements do not include all information and notes required by GAAP for complete financial statements, and should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the year ended December 31, 2006. The December 31, 2006 year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by GAAP. The financial information furnished reflects all adjustments, consisting only of normal recurring accruals, which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. The results of operations are not necessarily indicative of the results of operations that may be achieved in the future.

21st Century Holding Company (“21st Century,” “the Company,” “we,” “us”) is an insurance holding company, which, through our subsidiaries and our contractual relationships with our independent agents and general agents, controls substantially all aspects of the insurance underwriting, distribution and claims process. We are authorized to underwrite homeowners’ property and casualty insurance, commercial general liability insurance, and personal automobile insurance in various states with various lines of authority through our wholly owned subsidiaries, Federated National Insurance Company (“Federated National”) and American Vehicle Insurance Company (“American Vehicle”).

Federated National is authorized to underwrite homeowners’ property and casualty insurance and personal automobile insurance in Florida as an admitted carrier. American Vehicle is authorized to underwrite personal automobile insurance and commercial general liability coverage in Florida as an admitted carrier. In addition, American Vehicle is authorized to underwrite commercial general liability insurance in Georgia, Kentucky, South Carolina, Virginia, Missouri and Arkansas as a surplus lines carrier and in Texas, Louisiana and Alabama as an admitted carrier. American Vehicle operations in Florida, Georgia, Kentucky, Louisiana, Texas, South Carolina and Virginia are on-going. American Vehicle operations in Alabama, Arkansas and Missouri are expected to begin this year. American Vehicle has applications pending authorization as a surplus lines carrier in the states of California, Mississippi, Nevada and Maryland and an application pending submission as a surplus lines carrier to the state of Oklahoma.

During the six months ended June 30, 2007, 79.0%, 19.5% and 1.5% of the premiums we underwrote were for homeowners’ property and casualty insurance, commercial general liability insurance and personal automobile insurance, respectively. During the six months ended June 30, 2006, 75.2%, 19.1% and 5.7% of the premiums we underwrote were for homeowners’ property and casualty insurance, commercial general liability insurance and personal automobile insurance, respectively. We internally process claims made by our own and third-party insureds through our wholly owned claims adjusting company, Superior Adjusting, Inc. (“Superior”). We also offer premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium Finance, Inc. (“Federated Premium”).

We market and distribute our own and third-party insurers’ products and our other services primarily in Florida, through contractual relationships with a network of approximately 1,500 independent agents and a select number of general agents.

Assurance Managing General Agents, Inc. (“Assurance MGA”), a wholly owned subsidiary, acts as Federated National’s and American Vehicle’s exclusive managing general agent in the state of Florida. As American Vehicle continues its

expansion into other states we intend on retaining other general agents to market our commercial general liability insurance product beyond the state of Florida. Assurance MGA currently provides underwriting policy administration, marketing, accounting and financial services to Federated National and American Vehicle, and participates in the negotiation of reinsurance contracts. Assurance MGA generates revenue through a 6% commission fee from the insurance companies' gross written premium, policy fee income of \$25 per policy and other administrative fees from the marketing of company products through the Company's distribution network. The 6% commission fee from Federated National and American Vehicle was made effective January 1, 2005. Assurance MGA plans to establish relationships with additional carriers and add additional insurance products in the future.

21st Century Holding Company
Notes to Consolidated Financial Statements

(2) Summary of Significant Accounting Policies and Practices

(A) Critical Accounting Policies

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

The most significant accounting estimates inherent in the preparation of our financial statements include estimates associated with management's evaluation of the determination of liability for unpaid loss and loss adjustment expenses ("LAE") and the amount and recoverability of amortization of deferred policy acquisition costs. In addition, significant estimates form the basis for our reserves with respect to finance contracts, premiums receivable and deferred income taxes. Various assumptions and other factors underlie the determination of these significant estimates which are described in greater detail in Footnote 2 of the Company's audited financial statements for the fiscal year ended December 31, 2006 filed with the Securities and Exchange Commission ("SEC") on March 16, 2007.

The process of determining significant estimates is fact-specific and takes into account factors such as historical experience, current and expected economic conditions, and in the case of unpaid loss and LAE, an actuarial valuation. Management regularly reevaluates these significant factors and makes adjustments where facts and circumstances dictate. In selecting the best estimate, we utilize various actuarial methodologies. Each of these methodologies is designed to forecast the number of claims we will be called upon to pay and the amounts we will pay on average to settle those claims. In arriving at our best estimate, our actuaries consider the likely predictive value of the various loss development methodologies employed in light of underwriting practices, premium rate changes and claim settlement practices that may have occurred, and weight the credibility of each methodology. Our actuarial methodologies take into account various factors, including, but not limited to, paid losses, liability estimates for reported losses, paid allocated LAE, salvage and other recoveries received, reported claim counts, open claim counts and counts for claims closed with and without payment of loss.

Accounting for loss contingencies pursuant to Statements of Financial Accounting Standards ("SFAS"), No. 5 involves the existence of a condition, situation or set of circumstances involving uncertainty as to possible loss that will ultimately be resolved when one or more future event(s) occur or fail to occur. Additionally, accounting for a loss contingency requires management to assess each event as probable, reasonably possible or remote. Probable is defined as the future event or events are likely to occur. Reasonably possible is defined as the chance of the future event or events occurring is more than remote but less than probable, while remote is defined as the chance of the future event or events occurring is slight. An estimated loss in connection with a loss contingency shall be recorded by a charge to current operations if both of the following conditions are met: First, the amount can be reasonably estimated; and second, the information available prior to issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements. It is implicit in this condition that it is probable that one or more future events will occur confirming the fact of the loss or incurrence of a liability.

We are required to review the contractual terms of all our reinsurance purchases to ensure compliance with SFAS No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. The statement establishes the conditions required for a contract with a reinsurer to be accounted for as reinsurance and prescribes accounting and reporting standards for those contracts. Contracts that do not result in the reasonable possibility that the reinsurer may realize a significant loss from the insurance risk assumed generally do not meet the conditions for

reinsurance accounting and must be accounted for as deposits. SFAS No. 113 also requires us to disclose the nature, purpose and effect of reinsurance transactions, including the premium amounts associated with reinsurance assumed and ceded. It also requires disclosure of concentrations of credit risk associated with reinsurance receivables and prepaid reinsurance premiums.

(B) Impact of New Accounting Pronouncements

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21st Century Holding Company
Notes to Consolidated Financial Statements

In February 2007, the Financial Accounting Standards Board (“FASB”) issued SFAS No. 159 “*The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of SFAS No. 115*” (“SFAS No. 159”), which permits an entity to measure many financial assets and financial liabilities at fair value that are not currently required to be measured at fair value. Entities that elect the fair value option will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option may be elected on an instrument-by-instrument basis, with a few exceptions. SFAS No. 159 amends previous guidance to extend the use of the fair value option to available-for-sale and held-to-maturity securities. SFAS No. 159 also establishes presentation and disclosure requirements to help financial statement users understand the effect of the election. We will adopt SFAS No. 159 on its effective date, January 1, 2008. We do not expect the adoption of SFAS No. 159 to have a material impact, if any, on our financial position or results of operations.

In June 2006, FASB issued FIN 48, *Accounting for Uncertainty in Income Taxes* which clarifies the accounting for income tax reserves and contingencies recognized in an enterprise’s financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. The Company has evaluated and concluded that the impact of FIN 48 will be minimal and includes a policy of classifying interest and penalties related to income tax as elements of income tax expense in the consolidated financial statements. As required by FIN 48, this change was done prospectively. Previously, penalties and interest were classified as operating and underwriting expenses.

In December 2004, FASB revised SFAS No. 123, *Share-Based Payments* (“SFAS No. 123R”). This statement eliminates the option to apply the intrinsic value measurement provisions of the Accounting Principles Board (“APB”) No. 25 to stock compensation awards issued to employees. Rather, SFAS No. 123R requires companies to measure the cost of employee services received in exchange for an award of equity instruments based on the grant date fair value of the award. That cost will be recognized over the requisite service period (usually the vesting period) during which an employee is required to provide services in exchange for the award. SFAS No. 123R also requires companies to measure the cost of employee services received in exchange for employee stock purchase plan awards. SFAS No. 123R was effective for 21st Century’s fiscal year beginning January 1, 2006 as subsequently extended by the SEC pursuant to its April 13, 2005 announcement.

We have determined that the pretax charge to earnings for the year ending 2007 will total approximately \$0.6 million, of which approximately \$0.2 million was charged to income from continuing operations before provision for income taxes for the six months ended June 30, 2007. The effect on earnings per share for the six months ended June 30, 2007 for both undiluted and fully diluted was less than \$0.02 per share. For a more detailed discussion, please see Footnote 8, titled Stock Compensation Plans.

(C) Stock Options

At June 30, 2007, the Company had two stock-based employee compensation plans and one stock-based franchise compensation plan, which are described later in footnote 8, Stock Compensation Plans.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of SFAS No. 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized during the six months ended June 30, 2007 includes compensation cost for all share-based payments granted subsequent to January 1, 2007, based on the grant date fair-value estimated in accordance with the provisions of SFAS No. 123R.

During the six months ended June 30, 2007, we granted 30,000 qualified stock options to employees and 10,000 non-qualified stock options to a director with an average option price of \$12.42 per share. Like all other outstanding stock options, these stock options contain service conditions and do not contain any performance conditions. For a further discussion regarding the provisions of SFAS No. 123R and its effect on our operations, please refer to footnote 8, Stock Compensation Plans.

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21st Century Holding Company
Notes to Consolidated Financial Statements

(D) Earnings per Share

Basic earnings per share (“Basic EPS”) is computed by dividing net income by the weighted average number of common shares outstanding during the period presented. Diluted earnings per share (“Diluted EPS”) is computed by dividing net income by the weighted average number of shares of common stock and common stock equivalents outstanding during the period presented; outstanding warrants and stock options are considered common stock equivalents and are included in the calculation using the treasury stock method. Additionally, when applicable, we include in our computation of the weighted average number of common shares outstanding all common stock issued in connection with the repayment of our Subordinated note.

(E) Reclassifications

Certain amounts in 2006 financial statements have been reclassified to conform to the 2007 presentation.

(3) Revolving Credit Outstanding

Federated Premium’s operations are funded by a revolving loan agreement (“Revolving Agreement”) with FlatIron Funding Company LLC (“FlatIron”). The Revolving Agreement is structured as a sale of contracts receivable under a sale and assignment agreement with Westchester Premium Acceptance Corporation (“WPAC”) (a wholly-owned subsidiary of FlatIron), which gives WPAC the right to sell or assign these contracts receivable. Federated Premium, which services these contracts, has recorded transactions under the Revolving Agreement as secured borrowings. Outstanding borrowings under the Revolving Agreement as of June 30, 2007 and December 31, 2006 were unchanged at approximately \$10,000.

The effective interest rate on this line of credit, based on our average outstanding borrowings under the Revolving Agreement, was 20.22% and 14.4% for the three months ended June 30, 2007 and 2006, respectively. Interest expense on this revolving credit line for the three months ended June 30, 2007 and 2006 totaled approximately \$500 and \$3,400, respectively. Interest expense on this revolving credit line for the six months ended June 30, 2007 and 2006 totaled approximately \$1,000 and \$7,000, respectively.

(4) Commitments and Contingencies

Management has a responsibility to continually measure and monitor its commitments and its contingencies. The nature of the Company’s commitments and contingencies can be grouped into three major categories, insured claim activity, assessment related activities and operational matters.

We are involved in claims and legal actions arising in the ordinary course of business. Revisions to our estimates are based on our analysis of subsequent information that we receive regarding various factors, including: (i) per claim information; (ii) company and industry historical loss experience; (iii) legislative enactments, judicial decisions, legal developments in the awarding of damages, and (iv) trends in general economic conditions, including the effects of inflation. Management revises its estimates based on the results of its analysis. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for estimating the ultimate settlement of all claims. There is no precise method for subsequently evaluating the impact of any specific factor on the adequacy of the reserves, because the eventual redundancy or deficiency is affected by multiple factors. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations, or liquidity.

We operate in a regulatory environment where certain entities and organizations have the authority to require us to participate in assessments. Currently these entities and organizations include, but are not limited to, the Florida Joint Underwriters Association (“Florida JUA”), the Florida Insurance Guarantee Association (“FIGA”), Citizens Property Insurance Corporation (“Citizens”) and the Florida Hurricane Catastrophic Fund (“FHCF”).

As a direct premium writer in the State of Florida, we are required to participate in certain insurer solvency associations under Florida Statutes 631.57(3) (a). Participation in these pools is based on our written premiums by line of business compared to total premiums written statewide by all insurers. Participation may result in assessments against us as it did in 2006. During 2006 we were assessed \$3.9 million in connection with the FIGA. For statutory accounting purposes these assessments are not charged to operations, in contrast GAAP treatment is to charge current operations for the assessments. Through policyholder surcharges, as approved by the Florida Office of Insurance Regulation (“OIR”), during the six months ended June 30, 2007 we collected approximately \$681,000. These surcharges are reflected in other income in our statement of operations.

21st Century Holding Company
Notes to Consolidated Financial Statements

During its regularly scheduled meeting on August 17, 2005, the Board of Governors of Citizens determined a 2004 plan year deficit existed in the High Risk Account. Citizens decided that a \$515 million Regular Assessment was in the best interest of Citizens and consistent with Florida Statutes. On this basis, Citizens certified for a Regular Assessment. Federated National's participation in this assessment totaled \$2.0 million. During a subsequent regularly scheduled meeting on or about December 18, 2006, Citizens Board determined an additional 2004 plan year deficit existed in the High Risk Account. Citizens decided that an additional \$515 million Regular Assessment was in the best interest of Citizens and consistent with Florida Statutes. On this basis, Citizens certified for a Regular Assessment. Federated National's participation in this assessment totaled \$0.3 million. Provisions contained in our excess of loss reinsurance policies provide for reinsurance participation totaling \$1.5 million.

Pursuant to Section 627.3512, Florida Statutes, insurers are permitted to recoup the assessment by adding a surcharge to policies in an amount not to exceed the amount paid by the insurer to Citizens. Federated National is currently underwriting the recoupment in connection with these assessments and has recouped approximately \$0.2 million during the six months ended June 30, 2007. As noted above, Federated National continues to subrogate this assessment to our reinsurers.

The OIR issued Information Memorandum OIR-06-008M, titled *Notice of Anticipated Florida Hurricane Catastrophe Fund Assessment*, dated May 4, 2006, to all property and casualty, surplus lines insurers, and surplus lines agents in the state of Florida placing them on notice of an anticipated FHCF assessment. Sighting the unprecedented hurricane seasons of 2004 and 2005, the FHCF has exhausted nearly all of the \$6 billion in reserves it had accumulated since its inception in 1993. The Florida State Board of Administration, the body that oversees the FHCF, has issued its directive to levy an emergency assessment upon all property and casualty business in the state of Florida. There is no statutory requirement that policyholders be notified of the FCHF assessment. The FHCF and OIR are, however, recommending that insurers include the FHCF assessment in a line item on the declaration page for two reasons: (1) this is a multi-year assessment and (2) there may be concurrent assessments and the insureds should know what amount is for which assessment. The assessment became effective on all policies effective after January 1, 2007 and will be remitted to the administrator of the assessment as collected and therefore accounted for in a manner such that amounts collected or receivable are not recorded as revenues and amounts due or paid are not expensed.

In addition to the assessments noted above, the OIR has also issued Information Memorandum OIR -07-02M, titled *Information Regarding Emergency Assessment by Citizens Property Insurance Corporation*, dated January 11, 2007, to all property and casualty insurers in the state of Florida placing them on notice that an order has been approved for an emergency assessment by Citizens for its High Risk Account. This order requires insurers to begin collecting the emergency assessment for policies issued or renewed on or after July 1, 2007. Similar to the FHCF assessment discussed above, the Citizens emergency assessment will be remitted to the administrator of the assessment as collected and therefore accounted for in a manner such that amounts collected or receivable are not recorded as revenues and amounts due or paid are not expensed.

Both Federated National and American Vehicle participate in an insurance apportionment plan under Section 627.351, Florida Statutes, which is referred to as a Joint Underwriting Plan ("JUA Plan"). The JUA Plan provides for the equitable apportionment of any profits realized, or losses and expenses incurred, among participating motor vehicle insurers. In the event of an underwriting deficit incurred by the JUA Plan, which is not recovered through the policyholders in the JUA Plan, such deficit shall be recovered from the companies participating in the JUA Plan in the proportion that the net direct written premiums of each such member during the preceding calendar year bear to the aggregate net direct premiums written in this state by all members of the JUA Plan. During the six months ended June 30, 2007, Federated National and American Vehicle were not assessed by the JUA Plan based on their respective Cash Activity Reports. These assessments would be charged to operations as paid. Future assessments by this association

are undeterminable at this time.

The 2004, 2003 and 2002 consolidated Federal Income Tax Returns filed by the Company have been examined by the Internal Revenue Service (“IRS”) during 2006 and 2005. We have concurred with certain IRS conclusions and have appealed other conclusions. Irrespective of the ongoing appellate process, we do not believe that a material adjustment will occur. Income taxes receivable are net of \$160,000 reserve established in conjunction with this process.

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Relative to the Company's commitments stemming from operational matters, effective on or about March 1, 2006, 21st Century sold its interest in the Lauderdale Lakes property to an unrelated party. As part of this transaction, 21st Century has agreed to lease the same facilities for a five-year term. Our lease for this office space expires in December 2011.

The expected future lease payouts in connection with this lease are as follows:

| Fiscal Year | Lease payments |
|-------------|----------------|
| 2007 | \$ 301,443 |
| 2008 | 612,934 |
| 2009 | 625,193 |
| 2010 | 637,697 |
| 2011 | 650,451 |
| Total | \$ 2,827,718 |

On July 27, 2007 and August 7, 2007, two securities class action lawsuits were filed against the Company and certain of its executive officers in the United States District Court for the Southern District of Florida on behalf of all persons and entities who purchased the Company's securities between October 3, 2007 through May 3, 2007. While the specific factual allegations vary slightly in each case, the complaints allege that the defendants made false and misleading statements and failed to accurately project the Company's business and financial performance during the putative class period. The complaints seeks an unspecified amount of damages and claim violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. The Company expects that these two actions will be consolidated into one case in the United States District Court for the Southern District of Florida.

While the Company believes that the allegations in the complaint are without merit, an unfavorable resolution of pending litigation could have a material adverse effect on our financial condition. Litigation may result in substantial costs and expenses and significantly divert the attention of the Company's management regardless of the outcome. There can be no assurance that the Company will be able to achieve a favorable settlement of pending litigation or obtain a favorable resolution of this litigation if it is not settled. In addition, current litigation could lead to increased costs or interruptions of normal business operations of the Company.

(5) Comprehensive Income

For the three and six months ended June 30, 2007 and 2006, comprehensive income consisted of the following:

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|-------------------------------------|--------------|-----------------------------------|---------------|
| | 2007 | 2006 | 2007 | 2006 |
| Net income | \$ 10,478,429 | \$ 8,904,559 | \$ 11,321,234 | \$ 14,917,871 |
| Change in net unrealized gains on investments available for sale | (939,137) | (535,832) | (1,203,126) | (353,572) |
| Comprehensive income, before tax | 9,539,292 | 8,368,727 | 10,118,108 | 14,564,299 |
| Income tax benefit related to items of other comprehensive income | 430,812 | 201,634 | 530,151 | 133,049 |
| Comprehensive income | \$ 9,970,104 | \$ 8,570,361 | \$ 10,648,259 | \$ 14,697,348 |

(6) Segment Information

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FASB Statement No. 131, *Disclosures About Segments of an Enterprise and Related Information*, requires that the amount reported for each segment item be based on what is used by the chief operating decision maker in formulating a determination as to how many resources to assign to a segment and how to appraise the performance of that segment. The term chief operating decision maker may apply to the chief executive officer or chief operating officer or to a group of executives. Note: The term of chief operating decision maker may apply to a function and not necessarily to a specific person. This is a management approach rather than an industry approach in identifying segments. The segments are based on the Company's organizational structure, revenue sources, nature of activities, existence of responsible managers, and information presented to the Board of Directors.

A segment must be reported on if any one of the following exists:

- Revenue, including unaffiliated and inter-segment sales or transfers, is 10% or more of total revenue of all operating segments.
- Operating profit or loss is 10% or more of the greater, in absolute amount, of the combined operating profit (or loss) of all industry segments with operating profits (or losses).
 - Identifiable assets are 10% or more of total assets of all operating segments.

Operating segments that are not reportable should be combined and disclosed in the "all other" category. Disclosure should be made of the sources of revenue for these segments.

Accordingly, we have discontinued our segment disclosures for the finance segment, as it did not exceed the 10% threshold for revenues, earnings or assets.

(7) Reinsurance Agreements

We follow industry practice of reinsuring a portion of our risks and paying for that protection based primarily upon total insured values of all policies in effect and subject to such reinsurance. Reinsurance involves an insurance company transferring or "ceding" all or a portion of its exposure on insurance underwritten by it to another insurer, known as a "reinsurer." The ceding of insurance does not legally discharge the insurer from its primary liability for the full amount of the policies. If the reinsurer fails to meet its obligations under the reinsurance agreement, the ceding company is still required to pay the insured for the loss. Our reinsurance agreements are designed to coincide with the seasonality of Florida's hurricane season.

For the 2007-2008 hurricane season, the excess of loss and FHCF treaties will insure us for approximately \$403.0 million of aggregate loss and LAE with a maximum single event coverage totaling approximately \$320.0 million, with the Company retaining the first \$5.0 million of loss and LAE. Additionally, we purchased, Reinstatement Premium Protection from the private sector, which would reimburse the Company 100% of the cost of reinstatement for a second event. The FHCF affords coverage for the entire season, subject to maximum payouts, without regard to any particular insurable event. The cost to the Company for these reinsurance products for the 2007-2008 hurricane season, including the prepaid automatic premium reinstatement protection will be approximately \$40 million. The reinsurance companies and their respective A. M. Best Rating are noted in the table as follows:

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| Reinsurer | A.M. Best Rating |
|---|-------------------------|
| UNITED STATES | |
| Everest Reinsurance Company | A+ |
| Folksamerica Reinsurance Company | A- |
| GMAC Re/Motors Insurance Corporation | A- |
| Munich Reinsurance America, Inc. | A |
| Odyssey America Reinsurance Corporation | A |
| QBE Reinsurance Corporation | A |
| BERMUDA | |
| ACE Tempest Reinsurance Limited, Bermuda | A+ |
| Amlin Bermuda Limited | A- |
| Ariel Reinsurance Company Limited, Bermuda | A- |
| DaVinci Reinsurance Ltd, Bermuda | A |
| Flagstone Reinsurance Limited | A- |
| Max Bermuda Limited | A- |
| New Castle Reinsurance Company Limited | A- |
| Renaissance Reinsurance Ltd, Bermuda | A |
| UNITED KINGDOM | |
| Amlin Syndicate No. 2001 (AML) | A |
| Ascot Underwriting Syndicate No. 1414 (RTH) | A |
| G.S. Christensen and Others Syndicate No. 958 (GSC) | A |
| MAP Underwriting Syndicate No. 2791 (MAP) | A |
| Talbot Underwriting Syndicate No. 1183 (TAL) | A |
| EUROPE | |
| Converium Limited, Switzerland | B++ |

For the 2006-2007 hurricane season, we assembled a range of reinsurance products designed to insure the Company for an aggregate of approximately \$414.5 million for a minimum of two catastrophic events. The reinsurance treaties contained several complex features and through a series of fluid retentions, attachment points and limitations, additional coverage may have been afforded Federated National for events beyond the first two catastrophic events. Our retention would have varied depending on the severity and frequency of each catastrophic event. The reinsurance companies and their respective participation in the season's program are noted in the table as follows:

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| AM | | \$20m in excess of \$15m | First Event Participation \$40m in excess of \$35m | \$72m in excess of \$75m and FHCF participation | Reinstated Premium Protection \$20m in excess of \$15m | \$40m in excess of \$35m |
|-------------|---|--------------------------------------|---|---|---|--------------------------------|
| Best Rating | Reinsurer | | | | | |
| A+ | Ace Tempest Reinsurance Ltd | | 7.5% | 7.5% | | |
| A | Amlin 2001 Syndicate | 5.0% | 5.0% | 5.0% | 5.0% | |
| A- | Amlin Bermuda Ltd | 2.5% | 4.0% | 4.0% | 2.5% | |
| A | American Reinsurance Company | | | 3.5% | | |
| A | Ascot 1414 Syndicate | | | 6.5% | | |
| A++ | National Liability and Fire Company | | 33.8% | 6.6% | | 77.6% |
| B++ | Converium AG | | 5.0% | | | |
| A+ | Everest Reinsurance Company | | 22.0% | 4.3% | | 12.0% |
| NR | Wentworth Insurance Company Ltd | 5.0% | | . | 5.0% | |
| A- | Flagstone Reinsurance Ltd | | 4.3% | 4.0% | | |
| A | MAP 2791 Syndicate | 2.5% | 2.5% | 2.5% | 2.5% | |
| A- | New Castle Reinsurance Company Ltd | 2.0% | 2.0% | 2.0% | 2.0% | |
| A | QBE Reinsurance Corporation | | 1.5% | 1.0% | | |
| A | Renaissance Reinsurance, Ltd | | 12.5% | 12.5% | | |
| A+ | XL Re Limited | | | 2.5% | | |
| A | Odyssey | | | 3.5% | | |
| A | Catlin Insurance Company Ltd | 25.0% | | | 25.0% | |
| NR | Allianz Risk Transfer (Bermuda) Ltd | 33.0% | | | 33.0% | |
| A | Liberty Mutual Insurance Company American Vehicle Insurance | | | 34.7% | | |
| NR4 | Company (Affiliated) | 25.0% | | | 25.0% | |

In the discussion that follows it should be noted that all amounts of reinsurance were based on management's analysis of Federated National's exposure levels to catastrophic risk. Our data was subjected to exposure level data analysis at various dates through December 31, 2006.

Our overall reinsurance structure was divided into four major layers of financial impact in connection with any single catastrophic event. The bottom layer was considered to be the first \$15 million of losses. The next layer was considered to be greater than \$15 million and less than \$35 million. The next layer was considered to be greater than \$35 million and less than \$233.3 million. The fourth layer was considered losses greater than \$233.3 million and less than 305.3 million.

For the first and second catastrophic events equal to or less than \$15 million, the bottom layer, Federated National would have retained 100% of the first \$4.3 million and the last \$0.7 million of this bottom layer. The FHCF would have participated 100% for the \$10 million in excess of Federated National's first \$4.3 million.

For the first and second catastrophic events with aggregate losses in excess of the first \$15.0 million discussed above and less than \$35 million, Federated National acquired 100% reinsurance protection with a single automatic premium reinstatement protection provision. The \$20 million of coverage afforded in this layer was by way of a 42% traditional, single season, excess of loss ("Traditional") treaties and 58% structured multi-year, excess of loss ("Structured") treaties. As noted in the chart above, American Vehicle reinsured Federated National via a traditional treaty for 25% of this \$20 million layer. Relative to the structured excess of loss reinsurance treaties, terms contained in these treaties afford capacity in this layer beyond the 2006 - 2007 season for two additional hurricane seasons. The structured treaties offered respective coverage for a single event in each of the three hurricane seasons and one additional respective coverage that could be applied as needed in any one of the three hurricane seasons. One of the structured treaties, representing 25% of this layer, contained a provision which prevented the Company from recovery if any single event resulted in damages that exceed \$20 billion in the United States and its territories.

For the first and second catastrophic events where aggregate losses exceeded \$35 million, but were less than \$233.3 million, Federated National acquired 100% reinsurance protection through a combination of private market reinsurers and the FHCF program. The private market reinsurers afforded coverage to insure us for \$40 million against covered losses in excess of \$35 million. The FHCF afforded coverage to insure us for 90% of loss greater than \$55.6 million and less than \$231.5 million. The private treaties "wrapped around" the FHCF treaty afforded coverage, in aggregate, for losses in excess of \$35 million but less than \$233.3 million. The FHCF treaty was an aggregate "for the entire season" treaty while the private market treaties afforded respective per event coverage. As to reinstatement of coverage for the private market treaties, Federated National purchased a single automatic premium reinstatement protection provision that would have provided for an automatic reinstatement for 89% of the \$40 million coverage. Federated National would have been responsible for the remaining premium reinstatement protection and the cost in connection with that reinstatement was estimated to be approximately \$2.1 million. Federated National would also have been responsible for seasonal losses beyond what was afforded through this part of the FHCF coverage.

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If an event had occurred where aggregate losses exceed \$233.3 million, but were less than \$305.3 million, Federated National had acquired traditional reinsurance treaties representing 65.3% of this layer without a provision for premium reinstatement protection. Premium reinstatement coverage would have been prorated as to amount and if the first event exhausted this coverage then Federated National would have been responsible for approximately \$10.4 million for reinstatement protection. Additional coverage was afforded to Federated National via Industry Loss Warrants ("ILW"). The ILW policies provided for payments to Federated National based solely on industry wide losses to private and commercial property only in the State of Florida, notwithstanding losses incurred directly by Federated National. A payment to Federated National would only have been considered under the terms of these contracts, if insured wind damages incurred in the State of Florida had exceeded amounts varying between \$25 billion and \$20 billion excluding public property and certain other named exclusions.

The Company would have been responsible for single catastrophic events, with incurred losses in excess of approximately \$305 million subject to the terms of the ILW's above.

The estimated cost to the Company in connection with this reinsurance structure was approximately \$65 million, which for the most part was payable in quarterly installments that began July 1, 2006 and were amortized through earned premium in accordance with the provisions and terms contained in the respective treaties.

As a result of the loss and LAE incurred in connection with the hurricane activity that occurred in 2004 and 2005, the Company has reflected in its operations the effects of each storm as follows:

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| 2004 Hurricanes | Claim Count | Gross Losses | Reinsurance Recoveries | Net Losses |
|----------------------------|----------------|-----------------|---------------------------|----------------|
| (Dollars in millions) | | | | |
| Charley (August 13) | 2,572 | \$ 64.3 | \$ 54.3 | \$ 10.0 |
| Frances (September 3) | 3,809 | 53.4 | 43.3 | 10.1 |
| Ivan (September 14) | 1,062 | 26.5 | - | 26.5 |
| Jeanne (September 25) | 1,562 | 13.9 | - | 13.9 |
| Total Loss Estimate | 9,005 | \$ 158.1 | \$ 97.6 | \$ 60.5 |

| 2005 Hurricanes | Claim Count | Gross Losses | Reinsurance Recoveries | Net Losses |
|----------------------------|----------------|-----------------|---------------------------|---------------|
| (Dollars in millions) | | | | |
| Dennis (July 10) | 322 | \$ 2.8 | - | \$ 2.8 |
| Katrina (August 25) | 2,112 | 14.6 | 11.6 | 3.0 |
| Rita (September 20) | 19 | 0.1 | - | 0.1 |
| Wilma (October 24) | 11,696 | 174.5 | 171.5 | 3.0 |
| Total Loss Estimate | 14,149 | \$ 192.0 | \$ 183.1 | \$ 8.9 |

Effective March 28, 2006, American Vehicle entered into a 100% quota-share reinsurance treaty with Republic Underwriters Insurance Company ("Republic"). Republic is domiciled in the State of Texas and licensed both directly and on a surplus lines basis in approximately 32 states. Republic has a financial rating of "A-" Excellent with A.M. Best. This arrangement would have facilitated the policyholder who requires their commercial general liability insurance policy to come from an insurance company with an A.M. Best rating. Our arrangement with Republic allowed for a 4.75% commission on net written premium and reimbursement for all other costs in connection with the treaty such as premium taxes and assessments. We also remit a 1% commission to the intermediary broker on the same net written premium. Under this agreement the Company assumed approximately \$348,000 in premiums in connection with its operations in the State of Texas. Our operations in Texas began in December 2006. During the three months ended March 31, 2007, this 100% quota-sharing reinsurance treaty with Republic was cancelled at their request, effective June 30, 2007.

We are selective in choosing reinsurers and consider numerous factors, the most important of which are the financial stability of the reinsurer, their history of responding to claims and their overall reputation. In an effort to minimize our exposure to the insolvency of a reinsurer, we evaluate the acceptability and review the financial condition of the reinsurer at least annually.

Our automobile quota-share reinsurance treaties for 2003 include loss corridors with varying layers of coverage based on ultimate incurred loss ratio results whereby the two insurance companies will retain 100% of the losses between incurred loss ratios of 66% and 86% for policies with an effective date of 2003. Despite the loss corridor, the reinsurer assumes significant insurance risk under the reinsured portions of the underlying insurance contracts and it is reasonably possible that the reinsurer may realize a significant loss from the transaction. Our ultimate incurred loss ratios for these treaties as of December 31, 2006 are estimated to be 66.6% and 77.4% for Federated National and American Vehicle, respectively.

(8) Stock Compensation Plans

We implemented a stock option plan in November 1998 that provides for the granting of stock options to officers, directors, employees and consultants. The objectives of this plan include attracting and retaining the best personnel, providing for additional performance incentives, and promoting our success by providing employees the opportunity to acquire common stock. Options outstanding under this plan have been granted at prices that are either equal to or above the market value of the stock on the date of grant, typically vest over a four or five-year period, and expire ten years after the grant date. Under this plan, we are authorized to grant options to purchase up to 900,000 common shares, and, as of June 30, 2007 and December 31, 2006, we had outstanding exercisable options to purchase 82,750 and 44,750 shares, respectively.

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In 2001, we implemented a franchisee stock option plan that provided for the granting of stock options to individuals purchasing Company owned agencies which were then converted to franchised agencies. The purpose of the plan was to advance our interests by providing an additional incentive to encourage managers of Company owned agencies to purchase the agencies and convert them to franchises. Options outstanding under the plan were granted at prices which were above the market value of the stock on the date of grant, vest over a ten-year period, and expire ten years after the grant date. Under this plan, we are authorized to grant options to purchase up to 988,500 common shares, and, as of June 30, 2007, we had no outstanding exercisable options to purchase shares.

In 2002, we implemented the 2002 Option Plan. The purpose of this Plan is to advance our interests by providing an additional incentive to attract, retain and motivate highly qualified and competent persons who are key to the Company, including employees, consultants, independent contractors, and officers and directors, upon whose efforts and judgment our success is largely dependent, by authorizing the grant of options to purchase Common Stock to persons who are eligible to participate hereunder, thereby encouraging stock ownership by such persons, all upon and subject to the terms and conditions of the Plan. Options outstanding under the plan have been granted at prices which are above the market value of the stock on the date of grant, vest over a five-year period, and expire six years after the grant date. Under this plan, the Company is authorized to grant options to purchase up to 1,800,000 common shares, and, as of June 30, 2007 and December 31, 2006, we had outstanding exercisable options to purchase 619,658 and 637,358 shares, respectively.

Activity in the Company's stock option plans for the period from January 1, 2005 to June 30, 2007, is summarized below:

| | 1998 Plan | | 2001 Franchisee Plan | | 2002 Plan | |
|--------------------------------|------------------|--|----------------------|--|------------------|--|
| | Number of Shares | Weighted Average Option Exercise Price | Number of Shares | Weighted Average Option Exercise Price | Number of Shares | Weighted Average Option Exercise Price |
| Outstanding at January 1, 2005 | 198,275 | \$ 6.67 | 15,000 | \$ 9.17 | 906,300 | \$ 10.80 |
| Granted | - | \$ - | - | \$ - | 451,500 | \$ 14.39 |
| Exercised | (96,875) | \$ 6.67 | - | \$ - | (271,542) | \$ 8.96 |
| Cancelled | (3,750) | \$ 6.67 | - | \$ - | (262,650) | \$ 14.00 |
| Outstanding at January 1, 2006 | 97,650 | \$ 6.67 | 15,000 | \$ 9.17 | 823,608 | \$ 12.35 |
| Granted | 25,000 | \$ 27.79 | - | \$ - | 86,000 | \$ 16.44 |
| Exercised | (77,900) | \$ 6.67 | (15,000) | \$ 9.17 | (212,350) | \$ 8.98 |
| Cancelled | - | \$ - | - | \$ - | (59,900) | \$ 14.98 |
| Outstanding at January 1, 2007 | 44,750 | \$ 18.47 | - | \$ - | 637,358 | \$ 13.80 |
| Granted | 40,000 | \$ 12.42 | - | \$ - | - | \$ - |
| Exercised | (2,000) | \$ 6.67 | - | \$ - | (7,300) | \$ 10.38 |
| Cancelled | - | \$ - | - | \$ - | (10,400) | \$ 16.52 |
| Outstanding at June 30, 2007 | 82,750 | \$ 15.83 | - | \$ - | 619,658 | \$ 13.79 |

Options outstanding as of June 30, 2007 are exercisable as follows:

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| | 1998 Plan | | 2001 Franchisee Plan | | 2002 Plan | |
|----------------------------------|------------------|--|----------------------|--|------------------|--|
| | Number of Shares | Weighted Average Option Exercise Price | Number of Shares | Weighted Average Option Exercise Price | Number of Shares | Weighted Average Option Exercise Price |
| Options Exercisable at: | | | | | | |
| June 30, 2007 | 17,750 | \$ 15.83 | - | \$ - | 316,506 | \$ 13.79 |
| December 31, 2007 | 25,000 | \$ 15.83 | - | \$ - | 56,200 | \$ 13.79 |
| December 31, 2008 | 8,000 | \$ 15.83 | - | \$ - | 91,951 | \$ 13.79 |
| December 31, 2009 | 8,000 | \$ 15.83 | - | \$ - | 81,299 | \$ 13.79 |
| December 31, 2010 | 8,000 | \$ 15.83 | - | \$ - | 59,001 | \$ 13.79 |
| December 31, 2011 | 8,000 | \$ 15.83 | - | \$ - | 14,701 | \$ 13.79 |
| Thereafter | 8,000 | \$ 15.83 | - | \$ - | - | \$ 13.79 |
| Total options exercisable | 82,750 | | - | | 619,658 | |

At June 30, 2007, the Company has two stock-based employee compensation plans and one stock-based franchise compensation plan, which are described above. Prior to January 1, 2006, we accounted for those plans under the recognition and measurement provisions of stock-based compensation using the intrinsic value method prescribed by APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and related Interpretations, as permitted by FASB Statement No. 123, *Accounting for Stock-Based Compensation*. Under these provisions, no stock-based employee compensation cost was recognized in the Statement of Operations for the years ended December 31, 2005 or 2004 as all options granted under those plans had an exercise price equal to or less than the market value of the underlying common stock on the date of grant. Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB Statement No. 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized during the six months ended June 30, 2007 includes compensation cost for all share-based payments granted subsequent to January 1, 2007, based on the grant date fair-value estimated in accordance with the provisions of SFAS No. 123R. Results for prior periods have not been restated.

As a result of adopting SFAS No. 123R on January 1, 2006, the Company's income before provision for income taxes and net income for the six months ended June 30, 2007, are lower by approximately \$205,000 and \$143,000, respectively, than if it had continued to account for share-base compensation under ABP Opinion No. 25.

Basic and diluted earnings per share for the six-month period ended June 30, 2007 would have been \$1.44 and \$1.42, respectively, if the Company had not adopted SFAS No. 123R, as compared to reported basic and diluted earnings per share of \$1.42 and \$1.40, respectively.

Basic and diluted earnings per share for the three-month period ended June 30, 2007 would have been \$1.34 and \$1.33, respectively, if the Company had not adopted SFAS No. 123R, as compared to reported basic and diluted earnings per share of \$1.32 and \$1.31, respectively.

Because the change in income taxes payable includes the effect of excess tax benefits, those excess tax benefits also must be shown as a separate operating cash outflow so that operating cash flows exclude the effect of excess tax benefits. SFAS No. 123R requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows.

The weighted average fair value for the 40,000 new options granted during the three months ended June 30, 2007, estimated on the date of grant using the Black-Scholes option-pricing model was \$2.92 per option. There were no new options granted during the quarter ending June 30, 2006.

The fair value of options granted is estimated on the date of grant using the following assumptions:

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| | June 30, 2007 | June 30, 2006 |
|--------------------------|-----------------|-----------------|
| Dividend yield | 3.20% - 6.70% | 2.80% - 3.70% |
| Expected volatility | 42.87% - 54.77% | 43.97% - 44.30% |
| Risk-free interest rate | 4.79% to 4.86% | 5.18% |
| Expected life (in years) | 2.58 | 2.04 to 2.86 |

Volatility of a share price is the standard deviation of the continuously compounded rates of return on the share over a specified period of time. The higher the volatility, the more returns on the shares can be expected to vary - up or down. The expected volatility is a measure of the amount by which a financial variable such as a share price has fluctuated (historical volatility) or is expected to fluctuate (expected volatility) during a period. Our volatility as reflected above contemplates only historical volatility.

Summary information about the Company's stock options outstanding at June 30, 2007:

| | Range of Exercise Price | Outstanding at June 30, 2007 | Weighted Average Contractual Periods in Years | Weighted Average Exercise Price | Exercisable at June 30, 2007 |
|---------------------|----------------------------|---------------------------------|--|--|---------------------------------|
| 1998 Plan | \$6.67 - \$27.79 | 82,750 | 4.78 | \$15.83 | 17,750 |
| 2001 Franchise Plan | - | - | - | - | - |
| 2002 Plan | \$8.33 - \$18.21 | 619,658 | 3.11 | \$13.79 | 316,506 |

(9) Subordinated Debt

On July 31, 2003, we completed a private placement of our 6% Senior Subordinated Notes (the "July 2003 Notes"), which were offered and sold to accredited investors as units consisting of one July 2003 Note with a principal amount of \$1,000 and warrants (the "2003 Warrants") to purchase shares of our Common Stock. We sold an aggregate of \$7.5 million of July 2003 Notes in this placement, which resulted in proceeds to us (net of placement agent fees of \$450,724 and offering expenses of \$110,778) of \$6,938,498.

The July 2003 Notes paid interest at the annual rate of 6%, were subordinated to senior debt of the Company, and matured on July 31, 2006. Quarterly payments of principal and interest due on the July 2003 Notes were made in cash or, at our option, in shares of our Common Stock. When paid in shares of Common Stock, the number of shares issued was determined by dividing the payment due by 95% of the weighted-average volume price for the Common Stock on Nasdaq as reported by Bloomberg for the 20 consecutive trading days preceding the payment date.

The 2003 Warrants issued in this placement to the purchasers of the July 2003 Notes and to the placement agent in the offering, J. Giordano Securities Group ("J. Giordano"), each entitled the holder to purchase $\frac{3}{4}$ of one share of our Common Stock at an exercise price of \$12.744 per whole share (as adjusted for the Company's three-for-two stock split) until July 31, 2006. The total number of shares issuable upon exercise of 2003 Warrants issued to the purchasers of the July 2003 Notes and to J. Giordano totaled 612,074. GAAP required that detachable warrants be valued separately from debt and included in paid-in capital. Based on the terms of the purchase agreement with the investors in the private placement, management determined that the July 2003 Warrants had zero value at the date of issuance.

On July 31, 2006, we made the final principal payment of \$625,000 on the July 2003 notes and the July 2003 warrants expired. Of the 612,074 shares that could have been issued in connection with the July 2003 warrants, 301,430 were exercised, 225,000 were reacquired in the open market by us and 85,644 were unexercised. The unexercised warrants were cancelled as of July 31, 2006.

On September 30, 2004, we completed a private placement of 6% Senior Subordinated Notes due September 30, 2007 (the "September 2004 Notes"). These notes were offered and sold to accredited investors as units consisting of one September 2004 Note with a principal amount of \$1,000 and warrants to purchase shares of our Common Stock (the "2004 Warrants"), the terms of which are similar to our July 2003 Notes and 2003 Warrants, except as described below. We sold an aggregate of \$12.5 million of units in this placement, which resulted in proceeds (net of placement agent fees of \$700,000 and offering expenses of \$32,500) to us of \$11,767,500.

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Notes to Consolidated Financial Statements

The September 2004 Notes pay interest at the annual rate of 6%, mature on September 30, 2007, and rank pari passu in terms of payment and priority to the July 2003 Notes. Quarterly payments of principal and interest due on the September 2004 Notes, like the July 2003 Notes, may be made in cash or, at our option, in shares of our Common Stock. If paid in shares of Common Stock, the number of shares to be issued shall be determined by dividing the payment due by 95% of the weighted-average volume price for the Common Stock on Nasdaq as reported by Bloomberg for the 20 consecutive trading days preceding the payment date.

The 2004 Warrants issued to the purchasers of the September 2004 Notes and to the placement agent in the offering, J. Giordano, each entitle the holder to purchase one share of our Common Stock at an exercise price of \$12.75 per share and will be exercisable until September 30, 2007. The number of shares issuable upon exercise of the 2004 Warrants issued to purchasers equaled \$12.5 million divided by the exercise price of the warrants, and totaled 980,392. The number of shares issuable upon exercise of the 2004 Warrants issued to J. Giordano equaled \$500,000 divided by the exercise price of the warrants, and totaled 39,216. GAAP requires that detachable warrants be valued separately from debt and included in paid-in capital. Based on the terms of the purchase agreement with the investors in the private placement, management determined that the September 2004 Warrants had zero value at the date of issuance. Of the 1,019,000 warrants issued in connection with the September 2004 notes, 751,699 have been exercised to date.

The terms of the 2004 and 2003 Warrants provide for adjustment of the exercise price and the number of shares issuable thereunder upon the occurrence of certain events typical for private offerings of this type.

For the quarterly payment due April 30, 2006 we paid, pursuant to the terms of the July 2003 Notes and in accordance with the contractual computations 38,420 shares of our Common Stock for principal and interest.

As indicated on the table below, as of June 30, 2007, we paid, pursuant to the terms of the September 2004 Notes and in accordance with the contractual computations, selected quarterly payments of principal and interest due in shares of our Common Stock.

| Quarterly payment due date | 2007 | 2006 |
|----------------------------------|----------------|---------------|
| January 31, | 54,211 | - |
| April 30, | 63,114 | 68,696 |
| July 31, | - | - |
| October 31, | - | - |
| Total common stock issued | 117,325 | 68,696 |

The Company retains the privilege of repaying these notes in cash or by the issuance of common stock.

For the September 2004 Notes, the remaining quarterly principal and interest payments, totaling approximately \$1.0 million per payment, are due quarterly with the last installment due on September 30, 2007.

(10) Subsequent Event

On July 27, 2007 and August 7, 2007, two securities class action lawsuits were filed against the Company and certain of its executive officers in the United States District Court for the Southern District of Florida on behalf of all persons and entities who purchased the Company's securities between October 3, 2007 through May 3, 2007. While the

specific factual allegations vary slightly in each case, the complaints allege that the defendants made false and misleading statements and failed to accurately project the Company's business and financial performance during the putative class period. The complaints seeks an unspecified amount of damages and claim violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. The Company expects that these two actions will be consolidated into one case in the United States District Court for the Southern District of Florida.

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While the Company believes that the allegations in the complaint are without merit, an unfavorable resolution of pending litigation could have a material adverse effect on our financial condition. Litigation may result in substantial costs and expenses and significantly divert the attention of the Company's management regardless of the outcome. There can be no assurance that the Company will be able to achieve a favorable settlement of pending litigation or obtain a favorable resolution of this litigation if it is not settled. In addition, current litigation could lead to increased costs or interruptions of normal business operations of the Company.

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General information about 21st Century Holding Company can be found at www.21stcenturyholding.com however, the information that can be accessed through our web site is not part of our report. We make our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports filed or furnished pursuant to Section 13 or 15(d) of the Securities and Exchange Act of 1934 available free of charge on our web site, as soon as reasonably practicable after they are electronically filed with the SEC.

Item 2

Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

Statements in this Quarterly Report on Form 10-Q for the six months ended June 30, 2007 ("Form 10-Q") or in documents that are incorporated by reference that are not historical fact are forward-looking statements that are subject to certain risks and uncertainties that could cause actual events and results to differ materially from those discussed herein. Without limiting the generality of the foregoing, words such as "may," "will," "expect," "believe," "anticipate," "intend," "could," "would," "estimate," or "continue" or the negative other variations thereof or comparable terminology are intended to identify forward-looking statements. The risks and uncertainties include, without limitation, uncertainties related to estimates, assumptions and projections relating to losses from the nine hurricanes that occurred in fiscal years 2005 and 2004 and other estimates, assumptions and projections contained in this Form 10-Q; inflation and other changes in economic conditions (including changes in interest rates and financial markets); the impact of new regulations adopted in Florida which affect the property and casualty insurance market; pricing competition and other initiatives by competitors; ability to obtain regulatory approval for requested rate changes and the timing thereof; legislative and regulatory developments; the outcome of litigation pending against us, including the terms of any settlements; risks related to the nature of our business; dependence on investment income and the composition of our investment portfolio; the adequacy of our liability for loss and loss adjustment expense; insurance agents; claims experience; ratings by industry services; catastrophe losses; reliance on key personnel; weather conditions (including the severity and frequency of storms, hurricanes, tornadoes and hail); changes in driving patterns and loss trends; acts of war and terrorist activities; court decisions and trends in litigation and health care and auto repair costs; and other matters described from time to time by us in this report, and our other filings with the SEC.

You are cautioned not to place reliance on these forward-looking statements, which are valid only as of the date they were made. The Company undertakes no obligation to update or revise any forward-looking statements to reflect new information or the occurrence of unanticipated events or otherwise. In addition, readers should be aware that GAAP prescribes when a company may reserve for particular risks, including litigation exposures. Accordingly, results for a given reporting period could be significantly affected if and when a reserve is established for a major contingency. Reported results may therefore appear to be volatile in certain accounting periods.

Overview

We are an insurance holding company, which, through our subsidiaries and our contractual relationships with our independent agents and general agents, control substantially all aspects of the insurance underwriting, distribution and claims process. We are authorized to underwrite homeowners' property and casualty insurance, commercial general liability insurance, and personal automobile insurance, in various states with various lines of authority through our wholly owned subsidiaries, Federated National and American Vehicle. We internally process claims made by our own and third party insureds through our wholly owned claims adjusting company, Superior. We also offer premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium.

Federated National is authorized to underwrite homeowners' property and casualty insurance and personal automobile insurance in Florida as an admitted carrier. American Vehicle is authorized to underwrite personal automobile insurance and commercial general liability coverage in Florida as an admitted carrier. In addition, American Vehicle is authorized to underwrite commercial general liability insurance in Georgia, Kentucky, South Carolina, Virginia, Missouri and Arkansas as a surplus lines carrier and in Texas, Louisiana and Alabama as an admitted carrier. American Vehicle operations in Florida, Georgia, Kentucky, Louisiana, Texas, South Carolina and Virginia are on-going. American Vehicle operations in Alabama, Arkansas and Missouri are expected to begin this year. American Vehicle has applications pending authorization as a surplus lines carrier in the states of California, Mississippi, Nevada and Maryland and an application pending submission as a surplus lines carrier to the state of Oklahoma.

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During the six months ended June 30, 2007, 79.0%, 19.5% and 1.5% of the premiums we underwrote were for homeowners' property and casualty insurance, commercial general liability insurance and personal automobile insurance, respectively. During the six months ended June 30, 2006, 75.2%, 19.1% and 5.7% of the premiums we underwrote were for homeowners' property and casualty insurance, commercial general liability insurance and personal automobile insurance, respectively.

We market and distribute our own and third-party insurers' products and our other services primarily in Florida, through contractual relationships with a network of approximately 1,500 independent agents and a select number of general agents.

Assurance MGA, a wholly owned subsidiary, acts as Federated National's and American Vehicle's exclusive managing general agent in the state of Florida. Assurance MGA is not licensed to do business elsewhere. As American Vehicle continues its expansion into other states we intend on retaining other general agents to market our commercial general liability insurance product beyond the state of Florida. Assurance MGA currently provides underwriting policy administration, marketing, accounting and financial services to Federated National and American Vehicle, and participates in the negotiation of reinsurance contracts. Assurance MGA generates revenue through a 6% commission fee from the insurance companies' gross written premium, policy fee income of \$25 per policy and other administrative fees from the marketing of company products through the Company's distribution network. The 6% commission fee from Federated National and American Vehicle was made effective January 1, 2005. Assurance MGA plans to establish relationships with additional carriers and add additional insurance products in the future.

Our business, results of operations and financial condition are subject to fluctuations due to a variety of factors. Abnormally high severity or frequency of claims in any period could have a material adverse effect on our business, results of operations and financial condition. Also, if our estimated liabilities for unpaid losses and LAE are less than actual losses and LAE, we will be required to increase reserves with a corresponding reduction in our net income in the period in which the deficiency is identified.

We operate in highly competitive markets and face competition from national, regional and residual market insurance companies, many of whom are larger and have greater financial and other resources, have better ratings and offer more diversified insurance coverage. Our competitors include companies which market their products through agents, as well as companies which sell insurance directly to their customers. Large national writers may have certain competitive advantages over agency writers, including increased name recognition, increased loyalty of their customer base and reduced policy acquisition costs. Additionally, during an emergency session in January 2007, the Florida legislature passed and the Governor signed into law a bill known as "CS/HB-1A." This new law makes fundamental changes to the property and casualty insurance business in Florida and undertakes a multi-pronged approach to address the cost of residential property insurance in Florida. First, the new law requires insurance companies to lower their Florida premium rates for residential property insurance. The new law also authorizes the state-owned insurance company, Citizens, which is free of many of the restraints on private carriers such as surplus, ratios, income taxes and reinsurance expense, to reduce its premium rates and begin competing against private insurers in the residential property insurance market and expands the authority of Citizens to write commercial insurance. We may also face competition from new or temporary entrants in our niche markets. In some cases, such entrants may, because of inexperience, desire for new business or other reasons, price their insurance products below ours. Although our pricing is inevitably influenced to some degree by that of our competitors, we believe that it is generally not in our best interest to compete solely on price. We compete on the basis of underwriting criteria, our distribution network and superior service to our agents and insureds.

In Florida, more than 200 companies are authorized to underwrite homeowners' insurance. National and regional companies which compete with us in the homeowners' market include Allstate Insurance Company, State Farm Insurance Company, First Floridian Insurance Company, and Royal Palm Insurance Company. We also compete with several Florida domestic property and casualty companies such as Universal Insurance Company and Coral Insurance Company. During calendar year 2006, the Florida OIR announced the take over of several of our major competitors due to the poor financial condition stemming from the effects of the 2005 catastrophic hurricanes.

Comparable companies which compete with us in the commercial general liability insurance market include Century Surety Insurance Company, Atlantic Casualty Insurance Company, Colony Insurance Company and Burlington/First Financial Insurance Companies.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

With respect to automobile insurance in Florida, we compete with more than 100 companies, which underwrite personal automobile insurance. Comparable companies which compete with us in the personal automobile insurance market include Affirmative Insurance Holdings, Inc., which acquired our non-standard automobile agency business in Florida in December 2004, U.S. Security Insurance Company, United Automobile Insurance Company, Direct General Insurance Company and Security National Insurance Company, as well as major insurers such as Progressive Casualty Insurance Company.

Competition could have a material adverse effect on our business, results of operations and financial condition.

Our executive offices are located at 3661 West Oakland Park Boulevard, Suite 300, Lauderdale Lakes, Florida and our telephone number is (954) 581-9993.

Critical Accounting Policies

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions about future events that affect the amounts reported in the financial statements and accompanying notes. Future events and their effects cannot be determined with absolute certainty. Therefore, the determination of estimates requires the exercise of judgment. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

The most significant accounting estimates inherent in the preparation of our financial statements include estimates associated with management's evaluation of the determination of liability for unpaid loss and LAE and the amount and recoverability of amortization of deferred policy acquisition costs. In addition, significant estimates form the basis for our reserves with respect to finance contracts, premiums receivable and deferred income taxes. Various assumptions and other factors underlie the determination of these significant estimates which are described in greater detail in Footnote 2 of the Company's audited financial statements for the fiscal year ended December 31, 2006 filed with the SEC on March 16, 2007.

Except as described below, we believe that during the first six months of fiscal 2007 there were no significant changes in those critical accounting policies and estimates. Senior management has reviewed the development and selection of our critical accounting policies and estimates and their disclosure in this Form 10-Q with the Audit committee of our Board of Directors.

The process of determining significant estimates is fact specific and takes into account factors such as historical experience, current and expected economic conditions, and in the case of unpaid loss and LAE, an actuarial valuation. Management regularly reevaluates these significant factors and makes adjustments where facts and circumstances dictate. In selecting the best estimate, we utilize various actuarial methodologies. Each of these methodologies is designed to forecast the number of claims we will be called upon to pay and the amounts we will pay on average to settle those claims. In arriving at our best estimate, our actuaries consider the likely predictive value of the various loss development methodologies employed in light of underwriting practices, premium rate changes and claim settlement practices that may have occurred, and weight the credibility of each methodology. Our actuarial methodologies take into account various factors, including, but not limited to, paid losses, liability estimates for reported losses, paid allocated LAE, salvage and other recoveries received, reported claim counts, open claim counts and counts for claims closed with and without payment of loss.

Accounting for loss contingencies pursuant to SFAS No.5 involves the existence of a condition, situation or set of circumstances involving uncertainty as to possible loss that will ultimately be resolved when one or more future

event(s) occur or fail to occur. Additionally, accounting for a loss contingency requires management to assess each event as probable, reasonably possible or remote. Probable is defined as the future event or events are likely to occur. Reasonably possible is defined as the chance of the future event or events occurring is more than remote but less than probable, while remote is defined as the chance of the future event or events occurring is slight. An estimated loss in connection with a loss contingency shall be recorded by a charge to current operations if both of the following conditions are met: First, the amount can be reasonably estimated; and second, the information available prior to issuance of the financial statements indicates that it is probable that a liability has been incurred at the date of the financial statements. It is implicit in this condition that it is probable that one or more future events will occur confirming the fact of the loss or incurrence of a liability.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

We are required to review the contractual terms of all our reinsurance purchases to ensure compliance with SFAS No. 113, *Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*. The statement establishes the conditions required for a contract with a reinsurer to be accounted for as reinsurance and prescribes accounting and reporting standards for those contracts. Contracts that do not result in the reasonable possibility that the reinsurer may realize a significant loss from the insurance risk assumed generally do not meet the conditions for reinsurance accounting and must be accounted for as deposits. SFAS No. 113 also requires us to disclose the nature, purpose and effect of reinsurance transactions, including the premium amounts associated with reinsurance assumed and ceded. It also requires disclosure of concentrations of credit risk associated with reinsurance receivables and prepaid reinsurance premiums.

New Accounting Pronouncements

The material set forth in Item 1, Part I, "Financial Statements - Note 2 - Summary of Significant Accounting Policies and Practices" of this Form 10-Q is incorporated herein by reference.

In February 2007, the FASB issued SFAS No. 159 "*The Fair Value Option for Financial Assets and Financial Liabilities — Including an Amendment of SFAS No. 115*" ("SFAS No. 159"), which permits an entity to measure many financial assets and financial liabilities at fair value that are not currently required to be measured at fair value. Entities that elect the fair value option will report unrealized gains and losses in earnings at each subsequent reporting date. The fair value option may be elected on an instrument-by-instrument basis, with a few exceptions. SFAS No. 159 amends previous guidance to extend the use of the fair value option to available-for-sale and held-to-maturity securities. The Statement also establishes presentation and disclosure requirements to help financial statement users understand the effect of the election. We will adopt SFAS 159 on its effective date, January 1, 2008. We do not expect the adoption of SFAS 159 to have a material impact, if any, on our financial position or results of operations.

In June 2006, FASB issued FIN 48, *Accounting for Uncertainty in Income Taxes* which clarifies the accounting for income tax reserves and contingencies recognized in an enterprise's financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. This Interpretation also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. This Interpretation is effective for fiscal years beginning after December 15, 2006. The Company has adopted and concluded that the impact of FIN 48 will be minimal and includes a policy of classifying interest and penalties related to income tax as elements of income tax expense in the consolidated financial statements. As required by FIN 48, this change was done prospectively. Previously, penalties and interest were classified as operating and underwriting expenses.

Analysis of Financial Condition

As of June 30, 2007 as Compared to December 31, 2006

Total Investments

SFAS No. 115 addresses accounting and reporting for (a) investments in equity securities that have readily determinable fair values and (b) all investments in debt securities. SFAS 115 requires that these securities be classified into one of three categories, (i) held-to-maturity, (ii) trading securities or (iii) available-for-sale.

Investments classified as held-to-maturity include debt securities wherein the Company's intent and ability are to hold the investment until maturity. The accounting treatment for held-to-maturity investments is to carry them at amortized cost without consideration to unrealized gains or losses. Investments classified as trading securities include debt and

equity securities bought and held primarily for the sale in the near term. The accounting treatment for trading securities is to carry them at fair value with unrealized holding gains and losses included in current period operations. Investments classified as available-for-sale include debt and equity securities that are not classified as held-to-maturity or as trading security investments. The accounting treatment for available-for-sale securities is to carry them at fair value with unrealized holding gains and losses excluded from earnings and reported as a separate component of shareholders' equity, namely "Other Comprehensive Income".

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Total Investments increased \$31.2 million, or 25.0%, to \$156.1 million as of June 30, 2007, as compared to \$124.8 million as of December 31, 2006. The increase is primarily a result of our investment of the proceeds from an increase in written insurance premiums.

The fixed maturities and the equity securities that are available for sale and carried at fair value represent 86.9% of total investments as of June 30, 2007, as compared to 84.2% as of December 31, 2006.

We did not hold any non-traded investment securities during 2007 or 2006.

Below is a summary of net unrealized gains and (losses) at June 30, 2007 and December 31, 2006 by category.

| | Unrealized (Losses) and Gains | |
|--|-------------------------------|-------------------|
| | June 30, 2007 | December 31, 2006 |
| Fixed maturities: | | |
| U.S. government obligations and agency obligations | \$ (930,538) | \$ (688,190) |
| Obligations of states and political subdivisions | (184,715) | (145,505) |
| | (1,115,253) | (833,695) |
| Corporate securities: | | |
| Communications | 4,142 | 6,842 |
| Financial | (15,735) | (18,790) |
| Other | (176,561) | (73,983) |
| | (188,154) | (85,931) |
| Equity securities: | | |
| Common stocks | (1,450,345) | (631,000) |
| Total unrealized (losses) and gains, net | \$ (2,753,752) | \$ (1,550,626) |

During December 2005, we classified \$19.7 million of our bond portfolio as held-to-maturity. The decision to classify this layer of our bond portfolio as held-to-maturity was predicated on our intention to establish an irrevocable letter of credit in order to facilitate business opportunities in connection with our commercial general liability program. During April 2006, American Vehicle finalized the irrevocable letter of credit in conjunction with the 100% Quota Share Reinsurance Agreement with Republic.

Pursuant to FASB 115, the Company records the unrealized losses, net of estimated income taxes that are associated with that part of our portfolio classified as available for sale through the shareholders' equity account titled "Other Comprehensive Income". Management periodically reviews the individual investments that comprise our portfolio in order to determine whether a decline in fair value below our cost is either other than temporary or permanently impaired. Factors used in such consideration include, but are not limited to, the extent and length of time over which the market value has been less than cost, the financial condition and near-term prospects of the issuer and our ability and intent to keep the investment for a period sufficient to allow for an anticipated recovery in market value.

In reaching a conclusion that a security is either other than temporary or permanently impaired we consider such factors as the timeliness and completeness of expected dividends, principal and interest payments, ratings from nationally recognized statistical rating organizations such as Standard and Poor's and Moody's as well as information

released via the general media channels.

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Management's Discussion and Analysis of Financial Condition and Results of Operations

The investments held at June 30, 2007 and December 31, 2006 were comprised mainly of United States government and agency bonds as well as municipal bonds which are viewed by the Company as conservative and less risky holdings, though sensitive to interest rate changes. There is a smaller concentration of corporate bonds predominantly held in the financial and conglomerate industries. Approximately two-thirds of the equity holdings are in income funds while the other third is invested in equities related to the mortgage investment industry and business service industry.

All of our securities are in good standing and are not impaired as defined by FASB 115. We have determined that none of our securities qualify for other than temporary impairment or permanent impairment status. Our rationale for this determination includes, but is not limited, to Standard and Poor's rating of no less than BB++, no delinquent interest and dividend payments, near term maturity dates and our ability and intent to hold these securities for a period sufficient to allow for an anticipated recovery in market value.

Cash and Short Term Investments

Cash and short term investments, which include cash, certificates of deposits, and money market accounts decreased \$10.2 million, or 57.1%, to \$7.7 million as of June 30, 2007, as compared to \$17.9 million as of December 31, 2006. These balances are held primarily in money market accounts at amounts deemed sufficient to meet short-term cash requirements. Our excess cash and cash equivalents are invested in accordance with our long-term liquidity requirements.

Receivable for Investments Sold

Receivable for investments sold increased to \$5.0 million as of June 30, 2007, as compared to nothing as of December 31, 2006. The increase is a result of investment trading activity that occurred in late June and did not settle until early July 2007.

Finance Contracts Receivable, Net of Allowance for Credit Losses

Finance contracts receivable, net of allowance for credit losses, decreased \$0.3 million, or 19.0%, to \$1.5 million as of June 30, 2007, as compared to \$1.8 million as of December 31, 2006. The decrease is primarily due to our sale in December 2004 of our assets related to our non-standard automobile insurance agency business in Florida and the associated financed contracts. We anticipate a continued decline in the financed contracts receivable, net over the future short term and its related conversion to cash, cash equivalents and investments.

Prepaid Reinsurance Premiums

Prepaid reinsurance premiums decreased \$17.6 million, or 45.1%, to \$21.4 million as of June 30, 2007, as compared to \$38.9 million as of December 31, 2006. The decrease is due to our payments and amortization of prepaid reinsurance premiums associated with our homeowners' book of business.

Premiums Receivable, Net of Allowance for Credit Losses

Premiums receivable, net of allowance for credit losses, decreased \$0.2 million, or 2.4%, to \$7.0 million as of June 30, 2007, as compared to \$7.2 million as of December 31, 2006.

Our homeowners' insurance premiums receivable decreased \$1.7 million, or 41.2%, to \$2.5 million as of June 30, 2007, as compared to \$4.2 million as of December 31, 2006. The decrease can be attributed to the seasonality of the purchasing patterns of our policy holders.

Our commercial general liability insurance premiums receivable increased \$2.2 million, or 83.4%, to \$4.9 million as of June 30, 2007, as compared to \$2.7 million as of December 31, 2006.

Premiums receivable in connection with our automobile line of business decreased \$0.3 million, or 22.5%, to \$0.9 million as of June 30, 2007, as compared to \$1.2 million as of December 31, 2006.

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Reinsurance Recoverable

Reinsurance recoverable increased to \$3.0 million as of June 30, 2007, as compared to nothing as of December 31, 2006. The increase is due to the timing of settlements with our reinsurers in connection with the adjustment of loss and LAE claims as they relate to costs recoverable under our reinsurance agreements.

Deferred Policy Acquisition Costs

Deferred policy acquisition costs increased \$1.3 million, or 11.8%, to \$12.5 million as of June 30, 2007, as compared to \$11.2 million as of December 31, 2006. The increased production volume for both the homeowners' and commercial general liability product lines is the reason for the increase in this asset.

Deferred Income Taxes, net

Deferred income taxes, net, increased \$2.5 million, or 69.8%, to \$6.1 million as of June 30, 2007, as compared to \$3.6 million as of December 31, 2006. The increase is comprised primarily of \$2.3 million related to discounted unearned premiums and \$0.2 million in conjunction with other deferred tax assets, offset by \$0.5 million associated with deferred policy acquisition costs.

Income Taxes Receivable

Income taxes receivable increased \$0.3 million, or 40.1%, to \$1.1 million as of June 30, 2007, as compared to \$0.8 million as of December 31, 2006. The change is due to tax payment patterns in connection with our tax liabilities.

Property, Plant and Equipment, net

Property, plant and equipment, net, decreased \$0.1 million, or 9.6%, to \$1.2 million as of June 30, 2007, as compared to \$1.3 million as of December 31, 2006. The decrease is primarily due to depreciation and amortization of our existing property, plant and equipment.

Other Assets

Other assets increased \$6.2 million, or 135.1%, to \$10.7 million as of June 30, 2007, as compared to \$4.6 million as of December 31, 2006. Major components of other assets are as follows:

| | June 30, 2007 | December 31, 2006 |
|---|---------------|-------------------|
| Accrued interest income | \$ 1,713,615 | \$ 1,515,584 |
| Commissions and revenue sharing receivable | 7,278,117 | 979,677 |
| Notes receivable | 787,900 | 1,027,958 |
| Unamortized loan costs | 6,481 | 61,572 |
| Compensating cash balances | 9,911 | 9,911 |
| Due from sale of discontinued operations, net | 320,000 | 320,000 |
| Prepaid expenses | 476,393 | 531,008 |
| Other | 117,480 | 110,642 |
| | \$ 10,709,897 | \$ 4,556,352 |

The increase in commissions and revenue sharing receivable is primarily due to two separate and non-reoccurring operating events. First, pursuant to the terms in our three-year reinsurance treaties, we were afforded the right to cancel the remaining two years and receive a no loss experience commission. In connection with these treaties we have reported approximately \$2.8 million of commission income during the six months ended June 30, 2007. The second non-reoccurring operating event was \$2.4 million in commissions that we received from our participation in a Citizens take out program in May through July 2004, wherein the commissions were only earned upon the successful retention of the policyholders for thirty-six months.

Unpaid Losses and LAE

Unpaid losses and LAE increased \$5.6 million, or 14.1%, to \$45.2 million as of June 30, 2007, as compared to \$39.6 million as of December 31, 2006. The increase in unpaid losses and LAE relates to our payment patterns primarily relative to the settling of hurricane related claims. The composition of unpaid loss and LAE by product line is as follows:

| | June 30, 2007 | December 31, 2006 |
|------------------------------|---------------|-------------------|
| Homeowners' | \$ 26,735,894 | \$ 21,788,126 |
| Commercial General Liability | 13,534,474 | 11,100,116 |
| Automobile | 4,936,051 | 6,727,236 |
| | \$ 45,206,419 | \$ 39,615,478 |

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Factors that affect unpaid losses and LAE include the estimates made on a claim-by-claim basis known as "case reserves" coupled with bulk estimates known as incurred but not yet reported ("IBNR"). Periodic estimates by management of the ultimate costs required to settle all claim files are based on the Company's analysis of historical data and estimations of the impact of numerous factors such as (i) per claim information; (ii) company and industry historical loss experience; (iii) legislative enactments, judicial decisions, legal developments in the awarding of damages, and changes in political attitudes; and (iv) trends in general economic conditions, including the effects of inflation. Management revises its estimates based on the results of its analysis. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for estimating the ultimate settlement of all claims. There is no precise method for subsequently evaluating the impact of any specific factor on the adequacy of the reserves, because the eventual redundancy or deficiency is affected by multiple factors.

Unearned Premium

Unearned premiums increased \$12.8 million, or 16.5%, to \$90.7 million as of June 30, 2007, as compared to \$77.8 million as of December 31, 2006. The increase was due to a \$12.0 million increase in unearned homeowners' insurance premiums, a \$1.6 million increase in unearned commercial general liability premiums, and a \$0.7 million decrease in unearned automobile premiums. These changes reflect our continued emphasis in 2007 on property and commercial general liability insurance products.

Due to Reinsurers, net

Due to reinsurers, net decreased to nothing and converted to the asset reinsurance recoverable, net, as of June 30, 2007, as compared to \$4.2 million as of December 31, 2006.

Premium Deposits and Customer Credit Balances

Premium deposits and customer credit balances increased \$0.4 million, or 9.9%, to \$4.2 million as of June 30, 2007, as compared to \$3.8 million as of December 31, 2006. Premium deposits are monies received on policies not yet in force as of June 30, 2007.

Revolving Credit Outstanding

Revolving credit outstanding remained unchanged at nearly nothing as of June 30, 2007, as compared to December 31, 2006. The balance is due to our cash management efforts, our requested credit reduction, and sale in December 2004 of our assets related to our non-standard automobile insurance agency business in Florida and the derived finance contracts receivable.

Bank Overdraft

Bank overdraft increased \$2.5 million, or 30.4%, to \$10.6 million as of June 30, 2007, as compared to \$8.1 million as of December 31, 2006. The bank overdraft relates primarily to loss and LAE disbursements paid but not yet presented for payment by the policyholder or vendor. The increase relates to our payment patterns in relationship to the rate at which those cash disbursements are presented to the bank for payment.

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Subordinated Debt

Subordinated debt decreased \$2.1 million, or 50.0%, to \$2.1 million as of June 30, 2007, as compared to \$4.2 million as of December 31, 2006. The decrease is in connection with the scheduled quarterly principal payments on the September 2004 Notes.

Deferred Gain from Sale of Property

Deferred gain from sale of property decreased \$0.2 million, or 9.5%, to \$2.2 million as of June 30, 2007, as compared to \$2.5 million as of December 31, 2006. In accordance with the provisions of FASB No. 13, we are amortizing the deferred gain over the term of the lease-back which is scheduled to end in December 2011.

Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses decreased \$2.3 million, or 40.6%, to \$3.4 million as of June 30, 2007, as compared to \$5.7 million as of December 31, 2006. This decrease is due to our cash management efforts and timing of payments with our trade vendors.

Results of Operations

Three Months Ended June 30, 2007 as Compared to Three Months Ended June 30, 2006

Gross Premiums Written

Gross premiums written decreased \$6.3 million, or 12.4%, to \$44.5 million for the three months ended June 30, 2007, as compared to \$50.8 million for the three months ended June 30, 2006. The following table denotes gross premiums written by major product line:

| | 2007 | | Three months ended June 30, 2006 | |
|------------------------|---------------|------------|----------------------------------|------------|
| | Amount | Percentage | Amount | Percentage |
| Homeowners' | \$ 34,095,538 | 76.6% | \$ 41,855,449 | 82.5% |
| Commercial liability | 10,074,519 | 22.7% | 8,236,906 | 16.2% |
| Automobile | 291,447 | 0.7% | 660,317 | 1.3% |
| Gross premiums written | \$ 44,461,504 | 100.0% | \$ 50,752,672 | 100.0% |

The Company's sale of homeowners' policies decreased \$7.8 million, or 18.5% to \$34.1 million for the three months ended June 30, 2007, as compared to \$41.9 million for the three months ended June 30, 2006. The decrease is primarily due to the soft market conditions prevailing in the State of Florida lead by Citizens, the state run insurance company. We believe that the competition in this market is based primarily on pricing insurance products at rates that do not reflect current economic conditions. We do not intend to compete with others solely on the basis of pricing mechanisms. Where our rates are competitive (and there are territories in Florida that so exist) we will continue to market our property insurance product. We expect additional challenges in the near term in connection with our rating agency, Demotech, Inc.'s recent decision to remove our property insurer's financial stability rating "A" "Exceptional". We intend to discuss with Demotech, Inc. representatives corrective actions necessary to restore our rating.

The following table sets forth the amounts and percentages of our gross premiums written in connection with our commercial general liability program by state:

Three months ended June 30,

2007

2006

(Dollars in thousands)

| | 2007 | | 2006 | |
|------------------------|-----------|------------|----------|------------|
| | Amount | Percentage | Amount | Percentage |
| Florida | \$ 6,881 | 68.4% | \$ 6,174 | 75.0% |
| Georgia | 295 | 2.9% | 235 | 2.9% |
| Kentucky | 4 | 0.0% | - | 0.0% |
| Louisiana | 1,481 | 14.7% | 1,536 | 18.6% |
| South Carolina | 43 | 0.4% | - | 0.0% |
| Texas | 1,354 | 13.4% | 292 | 3.5% |
| Virginia | 17 | 0.2% | - | 0.0% |
| Gross premiums written | \$ 10,075 | 100.0% | \$ 8,237 | 100.0% |

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The Company's sale of auto insurance policies decreased by \$0.4 million, or 55.9%, to \$0.3 million for the three months ended June 30, 2007, as compared to \$0.7 million for the three months ended June 30, 2006.

Gross Premiums Ceded

Gross premiums ceded increased \$12.4 million, or 368.7%, to \$15.8 million for the three months ended June 30, 2007, as compared to \$3.4 million for the three months ended June 30, 2006.

(Decrease) in Prepaid Reinsurance Premiums

The (decrease) in prepaid reinsurance premiums was (\$0.8) million for the three months ended June 30, 2007, as compared to (\$0.6) million for the three months ended June 30, 2006. The increased charge to written premium is primarily associated with the timing of our reinsurance payments measured against the term of the underlying reinsurance policies.

(Increase) in Unearned Premiums

The (increase) in unearned premiums was (\$3.0) million for the three months ended June 30, 2007, as compared to (\$18.0) million for the three months ended June 30, 2006. The change was due to a (\$1.9) million increase in unearned homeowners' insurance premiums, a (\$1.8) million increase in unearned commercial general liability premiums and a \$0.6 million decrease in unearned automobile premiums. These changes reflect our continued growth along our homeowners' and commercial general liability lines of business.

Net Premiums Earned

Net premiums earned decreased \$3.9 million, or 13.7%, to \$24.8 million for the three months ended June 30, 2007, as compared to \$28.7 million for the three months ended June 30, 2006. The following table denotes net premiums earned by product line:

| | 2007 | | Three months ended June 30, 2006 | |
|----------------------|---------------|------------|----------------------------------|------------|
| | Amount | Percentage | Amount | Percentage |
| Homeowners' | \$ 15,540,961 | 32.94% | \$ 18,394,591 | 36.39% |
| Commercial liability | 8,403,025 | 17.81% | 6,515,591 | 12.89% |
| Automobile | 869,717 | 1.84% | 3,830,458 | 7.58% |
| Net premiums earned | \$ 24,813,703 | 52.59% | \$ 28,740,640 | 56.86% |

As noted above, the Company's efforts to expand commercial general liability lines of insurance products are coming to fruition, as reflected by increased net premiums earned of \$1.9 million, or 29.0 % to \$8.4 million for the three months ended June 30, 2007, as compared to \$6.5 million for the three months ended June 30, 2006.

Commission Income

Commission income increased \$6.4 million, to \$6.5 million for the three months ended June 30, 2007, as compared to \$0.1 million for the three months ending June 30, 2006. The primary components of our commission income are non-reoccurring operating events stemming from two separate events. First and pursuant to provisions contained in our three-year reinsurance treaties, we were afforded the right to cancel the remaining two years and receive a no loss

experience commission. In connection with these treaties we have reported approximately \$2.8 million in commission income during the three months ended June 30, 2007. The second non-reoccurring operating event was \$2.4 million in commissions that we received from our participation in a Citizens take out program in May through July 2004, wherein the commissions were only earned upon the successful retention of the policyholders for thirty-six months.

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Finance Revenue

Finance revenue decreased \$0.3 million, or 67.8%, to \$0.2 million for the three months ended June 30, 2007, as compared to \$0.5 million for the three months ended June 30, 2006. The change is primarily due to the Company's decreased emphasis on automobile insurance and the finance revenue derived there-from.

Managing General Agent Fees

Managing general agent fees increased 11.2% to \$0.8 million for the three months ended June 30, 2007, as compared to \$0.7 million for the three months ended June 30, 2006.

Net Investment Income

Net investment income increased \$0.5 million, or 32.2%, to \$2.1 million for the three months ended June 30, 2007, as compared to \$1.6 million for the three months ended June 30, 2006. The increase in investment income is primarily a result of the additional amounts of invested assets. Also affecting our net investment income was an increase in overall yield to 5.7 % for the three months ended June 30, 2007 as compared to a yield of 5.4% for the three months ended June 30, 2006.

Net Realized Investment Gains

Net realized investment gains decreased to \$0.1 million for the three months ended June 30, 2007, as compared to \$0.3 million for the three months ended June 30, 2006. The table below depicts gains by investment category.

| | Net Realized (Losses) Gains Three Months Ended June 30, | |
|--|--|-------------|
| | 2007 | 2006 |
| Fixed maturities: | | |
| Obligations of states and political subdivisions | \$ - | \$ (32,516) |
| Corporate securities: | | |
| Financial | - | - |
| Equity securities: | | |
| Common stocks | 80,087 | 315,857 |
| Total net realized (losses) gains | \$ 80,087 | \$ 283,341 |

Other Income

Other income decreased \$0.3 million, or 96.5%, to nearly nothing for the three months ended June 30, 2007, as compared to \$0.4 million for the three months ended June 30, 2006. Major components of other income for the three months ended June 30, 2007 included approximately \$0.4 million in connection with FIGA fees, \$0.1 million in partial recognition of our gain on the sale of our Lauderdale Lakes property and less than \$0.1 million in connection with rental and interest income. Offsetting the components totaling \$0.6 million was a \$0.6 million reclassification of commission income included as other income during the three months ended March 31, 2007.

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Loss and LAE

Loss and LAE, our most significant expense, represent actual payments made and changes in estimated future payments to be made to or on behalf of our policyholders, including expenses required to settle claims and losses. We revise our estimates based on the results of analysis of estimated future payments to be made. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for predicting future events.

Loss and LAE increased by \$0.3 million, or 3.4%, to \$9.7 million for the three months ended June 30, 2007, as compared to \$9.3 million for the three months ended June 30, 2006. The overall increase reflects an increase of \$1.1 million in our homeowners' loss and LAE program, an increase of \$2.5 million in our commercial general liability loss and LAE program netted against \$3.3 million decrease in loss and LAE in connection with our automobile program.

We continue to revise our estimates of the ultimate financial impact of past storms. The revisions to our estimates are based on our analysis of subsequent information that we receive regarding various factors, including: (i) per claim information; (ii) company and industry historical loss experience; (iii) legislative enactments, judicial decisions, legal developments in the awarding of damages, and (iv) trends in general economic conditions, including the effects of inflation. Management revises its estimates based on the results of its analysis. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for estimating the ultimate settlement of all claims. There is no precise method for subsequently evaluating the impact of any specific factor on the adequacy of the reserves, because the eventual redundancy or deficiency is affected by multiple factors.

The table below reflects no charge to operations during the three months ended June 30, 2007 from the four hurricanes that occurred in July, August, September and October of 2005.

| 2005 Hurricanes | Claim Count | Gross Losses | Reinsurance Recoveries (Dollars in millions) | Net Losses |
|----------------------------|----------------|-----------------|---|---------------|
| Dennis (July 10) | - | - | - | - |
| Katrina (August 25) | 2 | 0.1 | 0.1 | - |
| Rita (September 20) | - | - | - | - |
| Wilma (October 24) | 46 | (0.7) | (0.7) | - |
| Total Loss Estimate | 48 | \$(0.6) | \$(0.6) | - |

The table below reflects no charge to operations during the three months ended June 30, 2007 from the four hurricanes that occurred in July, August and September 2004.

| 2004 Hurricanes | Claim Count | Gross Losses | Reinsurance Recoveries (Dollars in millions) | Net Losses |
|-----------------------|----------------|-----------------|---|---------------|
| Charley (August 13) | - | 1.3 | 1.3 | - |
| Frances (September 3) | - | - | - | - |
| Ivan (September 14) | - | - | - | - |

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| | | | | |
|-----------------------|------|--------|--------|---|
| Jeanne (September 25) | - | - | - | - |
| Total Loss Estimate | - \$ | 1.3 \$ | 1.3 \$ | - |

In accordance with GAAP, our loss ratio is computed as loss and LAE divided by net premiums earned. A lower loss ratio generally results in higher operating income. Our loss ratio for the three month period ended June 30, 2007 was 38.9% compared with 32.5% for the same period in 2006. The table below reflects the loss ratios by product line.

| | Three Months Ended June 30, | |
|------------------------------|-----------------------------|-------|
| | 2007 | 2006 |
| Homeowners' | 37.5% | 25.8% |
| Commercial General Liability | 40.0% | 13.1% |
| Automobile | 54.7% | 97.7% |
| All lines | 38.9% | 32.5% |

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Management's Discussion and Analysis of Financial Condition and Results of Operations

Operating and Underwriting Expenses

Operating and underwriting expenses increased \$0.8 million, or 34.3%, to \$3.1 million for the three months ended June 30, 2007, as compared to \$2.3 million for the three months ended June 30, 2006. The increase is primarily due to the \$0.6 million increase in bad debts expense, which totaled \$0.7 million for the three months ended June 30, 2007, as compared to less than \$0.1 million for the three months ended June 30, 2006. Approximately \$0.3 million of the charge to bad debts expense during the three months ended March 31, 2007 was due to an increase in the allowance for doubtful accounts.

Salaries and Wages

Salaries and wages decreased less than \$0.1 million, or 2.2%, to \$1.7 million for the three months ended June 30, 2007, as compared to \$1.8 million for the three months ended June 30, 2006.

Interest Expense

Interest expense decreased \$0.1 million, or 66.8%, to \$0.1 million for the three months ended June 30, 2007, as compared to \$0.2 million for the three months ended June 30, 2006. The decrease is in correlation to our decreased subordinated debt.

Policy Acquisition Costs, Net of Amortization

Policy acquisition costs, net of amortization, increased \$0.8 million, or 18.9%, to \$4.9 million for the three months ended June 30, 2007, as compared to \$4.1 million for the three months ended June 30, 2006. Policy acquisition costs, net of amortization, consists of the actual policy acquisition costs, including commissions, payroll and premium taxes, less commissions earned on reinsurance ceded and policy fees earned.

Provision for Income Tax Expense

The provision for income tax expense decreased \$1.2 million, or 20.2%, to \$4.6 million for the three months ended June 30, 2007, as compared to \$5.7 million for the three months ended June 30, 2006. The effective rate for income tax expense was 30.3% for the three months ended June 30, 2007, as compared to 39.1% for the same three month period in 2006.

Net Income

As a result of the foregoing, the Company's net income for the three months ended June 30, 2007 was \$10.5 million, compared to net income of \$8.9 million for the three months ended June 30, 2006.

Results of Operations

Six Months Ended June 30, 2007 as Compared to Six Months Ended June 30, 2006

Gross Premiums Written

Gross premiums written increased \$7.3 million, or 8.4%, to \$93.7 million for the six months ended June 30, 2007, as compared to \$86.4 million for the six months ended June 30, 2006. The following table denotes gross premiums written by major product line:

| | Six months ended June 30, | | | |
|------------------------|---------------------------|------------|---------------|------------|
| | 2007 | | 2006 | |
| | Amount | Percentage | Amount | Percentage |
| Homeowners' | \$ 73,959,159 | 79.0% | \$ 64,957,975 | 75.2% |
| Commercial liability | 18,224,617 | 19.5% | 16,457,119 | 19.1% |
| Automobile | 1,468,457 | 1.5% | 4,946,651 | 5.7% |
| Gross premiums written | \$ 93,652,233 | 100.0% | \$ 86,361,745 | 100.0% |

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The following table sets forth the amounts and percentages of our gross premiums written in connection with our commercial general liability program by state:

| | Six months ended June 30, | | | |
|------------------------|---------------------------|------------|-----------|------------|
| | 2007 | | 2006 | |
| | Amount | Percentage | Amount | Percentage |
| | (Dollars in thousands) | | | |
| Florida | \$ 12,505 | 68.7% | \$ 12,741 | 77.4% |
| Georgia | 592 | 3.2% | 570 | 3.5% |
| Kentucky | 5 | 0.0% | - | 0.0% |
| Louisiana | 2,682 | 14.7% | 2,854 | 17.3% |
| South Carolina | 87 | 0.5% | - | 0.0% |
| Texas | 2,322 | 12.7% | 292 | 1.8% |
| Virginia | 32 | 0.2% | - | 0.0% |
| Gross premiums written | \$ 18,225 | 100.0% | \$ 16,457 | 100.0% |

The Company's sale of homeowners' policies increased \$9.0 million, or 13.9% to \$74.0 million for the six months ended June 30, 2007, as compared to \$65.0 million for the six months ended June 30, 2006. The increase is primarily due to the increased rates in effect on our homeowners' policies, and to a lesser extent, a greater number of in-force policies. We believe that the competition in this market is based primarily on pricing insurance products at rates that do not reflect current economic conditions. We do not intend to compete with others solely on the basis of pricing mechanisms. Where our rates are competitive (and there are territories in Florida that so exist) we will continue to market our property insurance product. We expect additional challenges in the near term in connection with our rating agency, Demotech, Inc.'s recent decision to remove our property insurer's financial stability rating "A" "Exceptional". We intend to discuss with Demotech, Inc. representatives corrective actions necessary to restore our rating.

The Company's sale of auto insurance policies decreased by \$3.5 million, or 70.3%, to \$1.5 million for the six months ended June 30, 2007, as compared to \$4.9 million for the six months ended June 30, 2006.

Gross Premiums Ceded

Gross premiums ceded increased \$12.4 million, or 368.9%, to \$15.8 million for the six months ended June 30, 2007, as compared to \$3.4 million for the six months ended June 30, 2006.

(Decrease) in Prepaid Reinsurance Premiums

The (decrease) in prepaid reinsurance premiums was (\$17.8) million for the six months ended June 30, 2007, as compared to (\$9.3) million for the six months ended June 30, 2006. The increased charge to written premium is primarily associated with the timing of our reinsurance payments measured against the term of the underlying reinsurance policies.

(Increase) in Unearned Premiums

The (increase) in unearned premiums was (\$12.8) million for the six months ended June 30, 2007, as compared to (\$23.2) million for the six months ended June 30, 2006. The change was due to a (\$12.0) million increase in unearned homeowners' insurance premiums, a (\$1.6) million increase in unearned commercial general liability premiums and a \$0.7 million decrease in unearned automobile premiums. These changes reflect our continued growth along our

homeowners' and commercial general liability lines of business.

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21st Century Holding Company**Net Premiums Earned**

Net premiums earned decreased \$3.4 million, or 6.6%, to \$47.2 million for the six months ended June 30, 2007, as compared to \$50.5 million for the six months ended June 30, 2006. The following table denotes net premiums earned by product line:

| | Six months ended June 30, | | | |
|----------------------------|---------------------------|----------------|----------------------|----------------|
| | 2007 | | 2006 | |
| | Amount | Percentage | Amount | Percentage |
| Homeowners' | \$ 28,351,819 | 60.08% | \$ 29,680,112 | 58.71% |
| Commercial liability | 16,668,739 | 35.33% | 12,382,467 | 24.50% |
| Automobile | 2,166,173 | 4.59% | 8,485,501 | 16.79% |
| Net premiums earned | \$ 47,186,731 | 100.00% | \$ 50,548,080 | 100.00% |

As noted above, the Company's efforts to expand commercial general liability lines of insurance products are coming to fruition, as reflected by increased net premiums earned of \$4.3 million, or 34.6 % to \$16.7 million for the six months ended June 30, 2007, as compared to \$12.4 million for the six months ended June 30, 2006.

Commissions Income

Commission income increased \$6.3 million, to \$6.5 million for the six months ended June 30, 2007 as compared to \$0.2 million for the six months ending June 30, 2006. The primary components of our commission income are non-reoccurring operating events stemming from two separate events. First and pursuant to provisions contained in our three-year reinsurance treaties, we were afforded the right to cancel the remaining two years and be entitled to receive a no loss experience commission. In connection with this treaty we have reported approximately \$2.8 million during the six months ended June 30, 2007. The second non-reoccurring operating event was in connection with commission income totaling approximately \$2.4 million in connection with a Citizens take out program in 2004, wherein the commission was only earned upon the successful retention of the policyholder for thirty-six months.

Finance Revenue

Finance revenue decreased \$0.8 million, or 69.4%, to \$0.3 million for the six months ended June 30, 2007, as compared to \$1.1 million for the six months ended June 30, 2006. The change is primarily due to the Company's decreased emphasis on automobile insurance and the finance revenue derived there-from.

Managing General Agent Fees

Managing general agent fees was unchanged at \$1.4 million for the six months ended June 30, 2007, as compared to \$1.4 million for the six months ended June 30, 2006.

Net Investment Income

Net investment income increased \$0.9 million, or 31.8%, to \$3.7 million for the six months ended June 30, 2007, as compared to \$2.8 million for the six months ended June 30, 2006. The increase in investment income is primarily a result of the additional amounts of invested assets. Also affecting our net investment income was an increase in overall yield to 5.3 % for the six months ended June 30, 2007 as compared to a yield of 4.8% for the six months ended

June 30, 2006.

Net Realized Investment (Losses) Gains

Net realized investment (losses) gains were nearly nothing for the six months ended June 30, 2007, as compared to \$0.5 for the six months ended June 30, 2006. The table below depicts (losses) gains by investment category.

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| | Net Realized (Losses) Gains Six Months Ended June 30, | |
|--|--|-------------|
| | 2007 | 2006 |
| Fixed maturities: | | |
| U.S. government obligations and agencies | \$ - | \$ (32,516) |
| Obligations of states and political subdivisions | (63) | 75 |
| | (63) | (32,441) |
| Corporate securities: | | |
| Other | - | (33,816) |
| Equity securities: | | |
| Common stocks | (47,982) | 545,809 |
| Total Net Realized (Losses) Gains | \$ (48,045) | \$ 479,552 |

Other Income

Other income increased less than \$0.1 million, or 3.2%, to \$1.0 million for the six months ended June 30, 2007, as compared to \$0.9 million for the six months ended June 30, 2006. Major components of other income for the six months ended June 30, 2007 included approximately \$0.7 million in connection with FIGA fees, \$0.2 million in partial recognition of our gain on the sale of our Lauderdale Lakes property and less than \$0.1 million of rental and interest income.

Loss and LAE

Loss and LAE, our most significant expense, represent actual payments made and changes in estimated future payments to be made to or on behalf of our policyholders, including expenses required to settle claims and losses. We revise our estimates based on the results of analysis of estimated future payments to be made. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for predicting future events.

Loss and LAE increased by \$6.8 million, or 40.5%, to \$23.8 million for the six months ended June 30, 2007, as compared to \$16.9 million for the six months ended June 30, 2006. The overall increase reflects an increase of \$7.2 million in our homeowners' loss and LAE program (including \$1.0 million charge for adverse development in connection with the 2004 hurricane season), an increase of \$3.8 million in our commercial general liability loss and LAE program netted against \$4.2 million decrease in loss and LAE in connection with our automobile program.

We continue to revise our estimates of the ultimate financial impact of past storms. The revisions to our estimates are based on our analysis of subsequent information that we receive regarding various factors, including: (i) per claim information; (ii) company and industry historical loss experience; (iii) legislative enactments, judicial decisions, legal developments in the awarding of damages, and (iv) trends in general economic conditions, including the effects of inflation. Management revises its estimates based on the results of its analysis. This process assumes that past experience, adjusted for the effects of current developments and anticipated trends, is an appropriate basis for estimating the ultimate settlement of all claims. There is no precise method for subsequently evaluating the impact of any specific factor on the adequacy of the reserves, because the eventual redundancy or deficiency is affected by multiple factors.

The table below reflects no charge to operations during the six months ended June 30, 2007 from the four hurricanes that occurred in July, August, September and October of 2005.

21st Century Holding Company

| 2005 Hurricanes | Claim Count | | Gross Losses | | Reinsurance Recoveries | | Net Losses |
|---------------------|----------------|----|-----------------------|----|---------------------------|----|---------------|
| | | | (Dollars in millions) | | | | |
| Dennis (July 10) | - | \$ | - | \$ | - | \$ | - |
| Katrina (August 25) | (1) | | 0.1 | | 0.1 | | - |
| Rita (September 20) | - | | - | | - | | - |
| Wilma (October 24) | 140 | | 10.5 | | 10.5 | | - |
| Total Loss Estimate | 139 | \$ | 10.6 | \$ | 10.6 | \$ | - |

The table below reflects a \$1.0 million charge to operations during the six months ended June 30, 2007 from the four hurricanes that occurred in July, August and September 2004.

| 2004 Hurricanes | Claim Count | | Gross Losses | | Reinsurance Recoveries | | Net Losses |
|-----------------------|----------------|----|-----------------------|----|---------------------------|----|---------------|
| | | | (Dollars in millions) | | | | |
| Charley (August 13) | 1 | \$ | 1.3 | \$ | 1.3 | \$ | - |
| Frances (September 3) | - | | - | | - | | - |
| Ivan (September 14) | - | | 1.0 | | - | | 1.0 |
| Jeanne (September 25) | - | | - | | - | | - |
| Total Loss Estimate | 1 | \$ | 2.3 | \$ | 1.3 | \$ | 1.0 |

In accordance with GAAP, our loss ratio is computed as loss and LAE divided by net premiums earned. A lower loss ratio generally results in higher operating income. Our loss ratio for the six month period ended June 30, 2007 was 50.3% compared with 33.5% for the same period in 2006. The table below reflects the loss ratios by product line.

| | Six Months Ended June 30, | |
|------------------------------|---------------------------|-------|
| | 2007 | 2006 |
| Homeowners' | 52.3% | 26.7% |
| Commercial General Liability | 36.1% | 17.6% |
| Automobile | 135.2% | 83.6% |
| All lines | 50.3% | 33.5% |

Operating and Underwriting Expenses

Operating and underwriting expenses increased \$2.5 million, or 53.2%, to \$7.1 million for the six months ended June 30, 2007, as compared to \$4.6 million for the six months ended June 30, 2006. The increase is due to the \$1.1 million increase in bad debts expense, which totaled \$1.3 million for the six months ended June 30, 2007, as compared to \$0.1 million for the six months ended June 30, 2006. Approximately \$0.4 million of the charge to bad debts expense during the six months ended June 30, 2007 was due to an increase in the allowance for doubtful accounts. The increase is also due to a charge to operations of \$1.0 million in connection with the tentative and expected to be negotiated settlement of an expired agreement to service insureds for a third-party insurance company. The terms of this agreement call for our company to adjust claims associated with policies of the third-party insurance company written between January 1, 2000 and December 31, 2001. The change is also due to a \$0.5 million increase in premium tax expense which is directly correlated to an increase in written premium.

Salaries and Wages

Salaries and wages decreased \$0.3 million, or 8.9%, to \$3.3 million for the six months ended June 30, 2007, as compared to \$3.6 million for the six months ended June 30, 2006.

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Interest Expense

Interest expense decreased \$0.3 million, or 64.6%, to \$0.1 million for the six months ended June 30, 2007, as compared to \$0.4 million for the six months ended June 30, 2006. The decrease is in correlation to our decreased subordinated debt.

Policy Acquisition Costs, Net of Amortization

Policy acquisition costs, net of amortization, increased \$1.5 million, or 18.3%, to \$9.5 million for the six months ended June 30, 2007, as compared to \$8.0 million for the six months ended June 30, 2006. Policy acquisition costs, net of amortization, consists of the actual policy acquisition costs, including commissions, payroll and premium taxes, less commissions earned on reinsurance ceded and policy fees earned.

Provision for Income Tax Expense

The provision for income tax expense decreased \$4.0 million, or 44.4%, to \$5.0 million for the six months ended June 30, 2007, as compared to \$8.9 million for the six months ended June 30, 2006. The effective rate for income tax expense was 30.6% for the six months ended June 30, 2007, as compared to 37.5% the same six month period in 2006.

Net Income

As a result of the foregoing, the Company's net income for the six months ended June 30, 2007 was \$11.3 million, compared to net income of \$14.9 million for the six months ended June 30, 2006.

Liquidity and Capital Resources

For the six months ended June 30, 2007, our primary sources of capital were revenues generated from operations, including decreased prepaid reinsurance premiums, increased unearned premiums, an increase in unpaid losses and LAE, increased bank overdraft and an increase in the provision for uncollectible premiums receivable. Operational sources of capital also included increased premium deposits and customer credit balances, decreased finance contracts receivable, depreciation and amortization, increased non-cash compensation and common stock issued for interest on notes. Also contributing to our liquidity were proceeds from the sale of investment securities, exercised employee stock options and a tax benefit related to non-cash compensation. Because we are a holding company, we are largely dependent upon fees and commissions from our subsidiaries for cash flow.

For the six months ended June 30, 2007, operations provided net operating cash flow of \$30.7 million, as compared to \$49.3 million for the six months ended June 30, 2006.

For the six months ended June 30, 2007, operations generated \$51.5 million of gross cash flow due to a \$17.6 million decrease in prepaid reinsurance premiums, a \$12.8 million increase in unearned premiums, a \$5.6 million increase in unpaid losses and LAE, a \$2.5 million increase in bank overdraft and a \$0.4 million increase in the provision for uncollectible premiums receivable. To a much less significant extent, operations generated additional sources of cash via a \$0.4 million increase in premium deposits and customer credit balances, a \$0.4 million decrease in finance contracts receivable, \$0.2 million in depreciation and amortization, \$0.1 million in non-cash compensation and \$0.1 million in common stock issued for interest on notes, all in conjunction with net income of \$11.3 million.

For the six months ended June 30, 2007, operations used \$20.8 million of gross cash flow primarily due to a \$7.3 million increase in reinsurance recoverable, net, a \$6.4 million increase in other assets, a \$2.5 million increase in deferred income tax expense, a \$2.3 million decrease in accounts payable and accrued expenses, a \$1.3 million increase in policy acquisition costs, net of amortization, a \$0.3 million increase in income taxes recoverable, a \$0.2 million increase in premiums receivable, \$0.2 million in amortization of investment discount, net, less than \$0.1 million in net realized investment losses and less than a \$0.1 million increase in the provision for credit losses, net.

Subject to catastrophic occurrences, net operating cash flow is currently expected to be positive in both the short-term and the reasonably foreseeable future.

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For the six months ended June 30, 2007, net investing activities used \$36.7 million, as compared to \$48.9 million for the six months ended June 30, 2006. Our available for sale investment portfolio is highly liquid as it consists entirely of readily marketable securities.

For the six months ended June 30, 2007, investing activities generated \$72.0 million and used \$108.7 million from the maturity several times over of our very short municipal portfolio.

For the six months ended June 30, 2007, net financing activities used \$4.2 million, as compared to providing \$3.5 million for the six months ended June 30, 2006. For the six months ended June 30, 2007, the sources of cash in connection with financing activities included \$0.1 million from the exercise of stock options and \$0.1 million from the tax benefit related to non-cash compensation. The uses of cash in connection with financing activities included \$2.9 million in dividends paid and \$1.5 million for the purchase of treasury stock.

Federated Premium's operations are partially funded by the revolving loan agreement with FlatIron. Outstanding borrowings under the revolving loan agreement were approximately \$10,000 as of both June 30, 2007 and December 31, 2006. The effective interest rate on this line of credit, based on our average outstanding borrowings under the revolving loan agreement, was 20.22% and 14.4% for the six months ended June 30, 2007 and 2006, respectively. Interest expense on this revolving credit line totaled approximately \$1,000 and \$7,000 for the six months ended June 30, 2007 and 2006, respectively.

As an alternative to premium finance, we offer direct billing in connection with our automobile program, where the insurance company accepts from the insured, as a receivable, a promise to pay the premium, as opposed to requiring the full amount of the policy, either directly from the insured or from a premium finance company. The advantage of direct billing a policyholder by the insurance company is that we are not reliant on our credit facility, but remain able to charge and collect interest from the policyholder.

We believe that our current capital resources, together with cash flow from operations, will be sufficient to meet currently anticipated working capital requirements. There can be no assurances, however, that such will be the case.

As of June 30, 2007, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as "structured finance" or "special purpose" entities, which were established for the purpose of facilitating off-balance-sheet arrangements or other contractually narrow or limited purposes. As such, management believes that we currently are not exposed to any financing, liquidity, market or credit risks that could arise if we had engaged in transactions of that type requiring disclosure herein.

Impact of Inflation and Changing Prices

The consolidated financial statements and related data presented herein have been prepared in accordance with GAAP which requires the measurement of financial position and operating results in terms of historical dollars without considering changes in the relative purchasing power of money over time due to inflation. Our primary assets and liabilities are monetary in nature. As a result, interest rates have a more significant impact on performance than the effects of general levels of inflation. Interest rates do not necessarily move in the same direction or with the same magnitude as the inflationary effect on the cost of paying losses and LAE.

Insurance premiums are established before we know the amount of loss and LAE and the extent to which inflation may affect such expenses. Consequently, we attempt to anticipate the future impact of inflation when establishing rate levels. While we attempt to charge adequate premiums, we may be limited in raising premium levels for competitive

and regulatory reasons. Inflation also affects the market value of our investment portfolio and the investment rate of return. Any future economic changes which result in prolonged and increasing levels of inflation could cause increases in the dollar amount of incurred loss and LAE and thereby materially adversely affect future liability requirements.

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Item 3

Quantitative and Qualitative Disclosures about Market Risk

Information related to quantitative and qualitative disclosures about market risk was included under Item 7a, “Quantitative and Qualitative Disclosures about Market Risk”, in our Annual Report on Form 10-K for the year ended December 31, 2006. No material changes have occurred in market risk since this information was disclosed except as discussed below.

Our investment portfolio is available for sale and carried at fair value, except for that portion deemed as held to maturity. Gains that represent securities with a fair value in excess of amortized cost, and losses (amortized cost is in excess of fair value) that are deemed temporary by management are recorded in shareholders’ equity in accumulated other comprehensive income. Losses deemed other than temporary by management are recorded as net realized losses in the consolidated statement of operations. A summary of the investment portfolio as of June 30, 2007 follows:

| | Book Value | | Fair / Amortized Value | | Unrealized Gain(Loss) |
|---|----------------|---------|------------------------|---------|-----------------------|
| Fixed maturities: | | | | | |
| U.S. government obligations and agencies available for sale | \$ 81,077,632 | 51.05% | \$ 80,147,095 | 51.36% | \$ (930,537) |
| U.S. government obligations and agencies held to maturity | 19,371,569 | 12.20% | 19,371,567 | 12.41% | (2) |
| Obligations of states and political subdivisions available for sale | 49,009,647 | 30.86% | 48,824,931 | 31.29% | (184,716) |
| Obligations of states and political subdivisions held to maturity | 501,355 | 0.32% | 501,355 | 0.32% | - |
| | 149,960,203 | 94.43% | 148,844,948 | 95.38% | (1,115,255) |
| Corporate securities: | | | | | |
| Communications available for sale | 507,508 | 0.34% | 511,652 | 0.33% | 4,144 |
| Financial available for sale | 500,000 | 0.31% | 484,265 | 0.31% | (15,735) |
| Other available for sale | 1,650,000 | 1.04% | 1,473,439 | 0.94% | (176,561) |
| Other held to maturity | 500,000 | 0.31% | 500,000 | 0.32% | - |
| | 3,157,508 | 2.00% | 2,969,356 | 1.90% | (188,152) |
| Equity securities: | | | | | |
| Common stocks available for sale | 5,699,858 | 3.57% | 4,249,513 | 2.72% | (1,450,345) |
| Total fixed, corporate and equity securities | \$ 158,817,569 | 100.00% | \$ 156,063,817 | 100.00% | \$ (2,753,752) |

For our held to maturity portfolio as of June 30, 2007, the unrealized loss totaled approximately \$98,000 and was in connection with our U.S. government obligations and agencies.

As of June 30, 2007, there were no concentrations greater than 5% of total investments in any single investment other than United States government and agency obligations and obligations of states and political subdivisions.

Item 4

Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that the Company files or submits under the Securities and Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC's rules and forms, and that such information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosures.

Our management, with the participation of its Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as defined in Rules 13a-15(e) under the Securities Exchange Act of 1934, as of June 30, 2007. Based upon their evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures, as of June 30, 2007, were effective to provide reasonable assurance that information required to be disclosed by the Company in the reports filed or submitted by it under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and to provide reasonable assurance that information required to be disclosed by the Company in such reports is accumulated and communicated to our management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

21st Century Holding Company

Our Company assesses the adequacy of its internal control over financial reporting quarterly and strives to enhance its controls in response to internal control assessments and external audit recommendations. No control enhancements during the quarter ended June 30, 2007 or through the date of this Form 10-Q have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting except as stated in the following paragraph.

In our Form 10-K for the fiscal year ended December 31, 2006, the Company had two "material weaknesses" in our internal control over financial reporting with respect to (i) the recognition and accounting of unrecorded premium transactions and (ii) an income tax issue relating to computing our income tax liability where we failed to consider a prior year tax refund applied to our fiscal year ended December 31, 2006.

We continue our efforts to remediate these material weaknesses through ongoing process improvements and the implementation of enhanced policies and controls over the timely recognition of unreported premium transactions and tax accounting in fiscal 2007, and such remediation will continue during the remaining part of fiscal 2007. Accordingly, these material weaknesses have yet to be fully remediated and tested.

To compensate for these material weaknesses, the Company performed additional analysis and other procedures in order to prepare the unaudited quarterly consolidated financial statements in accordance with generally accepted accounting principles in the United States of America. Accordingly, management believes that the unaudited consolidated financial statements included in this Form 10-Q fairly present, in all material respects, our financial condition, results of operations and cash flows for the periods presented.

Except for our ongoing remediation efforts, there were no changes during the quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II: OTHER INFORMATION

Item 1

Legal Proceedings

We are involved in various claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations, or liquidity.

On July 27, 2007 and August 7, 2007, two securities class action lawsuits were filed against the Company and certain of its executive officers in the United States District Court for the Southern District of Florida on behalf of all persons and entities who purchased the Company's securities between October 3, 2007 through May 3, 2007. While the specific factual allegations vary slightly in each case, the complaints allege that the defendants made false and misleading statements and failed to accurately project the Company's business and financial performance during the putative class period. The complaints seeks an unspecified amount of damages and claim violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. The Company expects that these two actions will be consolidated into one case in the United States District Court for the Southern District of Florida.

The Company believes the allegations are without merit, and intends to vigorously defend this class action lawsuit. There can be no assurance regarding the ultimate outcome of this matter, or the significance, if any, to the Company's business, consolidated results of operations or financial position.

Item 1A

Risk Factors

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2006 and the risk factors set forth below, which could materially affect our business, financial condition or future results. The risks described in our Annual Report on Form 10-K and this Form 10-Q are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition and/or operating results. The most significant of these risks include weather related conditions.

We are named as a defendant in two securities class action lawsuits and it may have an adverse impact on our business

On July 27, 2007 and August 7, 2007, two securities class action lawsuits were filed against the Company and certain of its executive officers in the United States District Court for the Southern District of Florida on behalf of all persons and entities who purchased the Company's securities between October 3, 2007 through May 3, 2007. While the specific factual allegations vary slightly in each case, the complaints allege that the defendants made false and misleading statements and failed to accurately project the Company's business and financial performance during the putative class period. The complaints seeks an unspecified amount of damages and claim violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5. The Company expects that these two actions will be consolidated into one case in the United States District Court for the Southern District of Florida.

While the Company believes that the allegations in the complaint are without merit, an unfavorable resolution of pending litigation could have a material adverse effect on our financial condition. Litigation may result in substantial costs and expenses and significantly divert the attention of the Company's management regardless of the outcome. There can be no assurance that the Company will be able to achieve a favorable settlement of pending litigation or obtain a favorable resolution of this litigation if it is not settled. In addition, current litigation could lead to increased costs or interruptions of normal business operations of the Company.

Adverse ratings by insurance rating agencies may adversely impact our ability to write new policies, renew desirable policies or obtain adequate insurance, which could limit or halt our growth and harm our business.

Third-party rating agencies assess and rate the ability of insurers to pay their claims. These financial strength ratings are used by the insurance industry to assess the financial strength and quality of insurers. These ratings are based on criteria established by the rating agencies and reflect evaluations of each insurer's profitability, debt and cash levels, customer base, adequacy and soundness of reinsurance, quality and estimated market value of assets, adequacy of reserves, and management. Ratings are based upon factors of concern to agents, reinsurers and policyholders and are not directed toward the protection of investors, such as purchasers of our common stock.

21st Century Holding Company

There are a number of companies which currently rate insurance companies. American Vehicle is currently rated by Demotech with a rating of “A” “*Exceptional*”. In July 2007, we were advised by Demotech that it was unwilling to assign a preliminary financial stability rating at the “A” “*Exceptional*” level to Federated National.

We were rated by A.M. Best until August 2004, but we requested that it stop rating Federated National and American Vehicle when these entities were placed under review with negative implications. We expect that this may negatively impact our ability to compete in the property and casualty market in Florida.

Item 2**(a) Unregistered Sales of Equity Securities and Use of Proceeds**

During the three months ended June 30, 2007, certain non-executive employees exercised options to acquire an aggregate of 1,200 shares of the Company's common stock with proceeds to the Company aggregating to approximately \$11,000. All of the option holders paid cash for these shares. The shares underlying the options were registered on registration statements on Form S-8 and the shares issued to these persons do not contain any restrictive legends.

During May and June 2007, we issued an aggregate 30,000 options to an employee, an officer and a director of the Company under our 1998 stock option plan. The options have an exercise price between \$11.11 and \$11.33 per share, vest over five years at 20% per year and expire six years from the grant date.

(b) None**(c) Market for the Company's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities**

On May 14, 2007, the Company's Board of Directors authorized, pursuant to Section 12 of the Securities Exchange Act, the repurchase of up to \$5.0 million of its common stock. Acting upon the Board's authorization, the Company repurchased, for approximately \$1.5 million, 138,261 shares for an average price of \$10.99 between May 16, 2007 and May 21, 2007. The table below provides, in tabular format, information about our purchase of equity securities that are registered by the Company.

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plan |
|----------|--|------------------------------------|--|--|
| April-07 | None | None | None | None |
| May-07 | 138,261 | \$ 10.99 | 138,261 | \$3.5 million |
| June-07 | None | None | None | \$3.5 million |

Item 3**Defaults upon Senior Securities**

None

Item 4

Submission of Matters to a Vote of Security Holders

Our annual meeting of shareholders was held on May 22, 2007. Proxies for the meeting were solicited pursuant to Regulation 14A of the Securities Exchange Act of 1934 and there was no solicitation in opposition to that of management.

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21st Century Holding Company

Both of management's nominees for directors as listed in the proxy statement were elected. Edward J. Lawson and Michael H. Braun were elected as Class I directors to serve until the Annual Shareholder's Meeting to be held in 2010 or until their successors are qualified and elected. The number of votes cast for each nominee is as follows:

| | Shares Voted "FOR" | Votes Withheld |
|------------------|-----------------------|-------------------|
| Edward J. Lawson | 6,066,647 | 503,605 |
| Michael H. Braun | 6,076,616 | 493,636 |

The proposal to approve the appointment of DeMeo Young McGrath as the Company's independent auditors for the fiscal year ended December 31, 2007, was ratified by the following votes:

| Shares Voted "FOR" | Shares Voted "AGAINST" | Shares "ABSTAINING" | Broker "NON-VOTE" |
|-----------------------|---------------------------|------------------------|----------------------|
| 6,433,958 | 106,175 | 30,118 | 1 |

Item 5**Other Information**

None

Item 6**Exhibits**

10.1 Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF), effective June 1, 2007 (incorporated by reference to Exhibit 10.1 contained in the Company's Form 8-K filed on June 1, 2007).

10.2 Addendums Number 1 to the Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF), effective June 1, 2007 (incorporated by reference to Exhibit 10.2 contained in the Company's Form 8-K filed on June 1, 2007).

10.3 Addendum No. 2 to the Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF), effective June 1, 2007 (incorporated by reference to Exhibit 10.3 contained in the Company's Form 8-K filed on June 1, 2007).

10.4 Addendum No. 3 to the Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF), effective June 1, 2007 (incorporated by reference to Exhibit 10.4 contained in the Company's Form 8-K filed on June 1, 2007).

10.5 Addendum No. 4 to the Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF), effective June 1, 2007 (incorporated by reference to Exhibit 10.5 contained in the Company's Form 8-K filed on June 1, 2007).

10.6 Employment Agreement between the Company and Peter J. Prygelski, effective June 25, 2007 (incorporated by reference to Exhibit 10.1 contained in the Company's Form 8-K filed on June 19, 2007).

10.7 Annual Review Agreement between the Company and Peter J. Prygelski, effective June 25, 2007 (incorporated by reference to Exhibit 10.2 contained in the Company's Form 8-K filed on June 19, 2007).

21st Century Holding Company

- 10.8 Non-Compete Agreement between the Company and Peter J. Prygelski, effective June 25, 2007 (incorporated by reference to Exhibit 10.3 contained in the Company's Form 8-K filed on June 19, 2007)
- 10.9 Indemnification Agreement between the Company and Anthony C. Kryer, III dated June 25, 2007. *
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act. *
- 31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act. *
- 32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act. *
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act. *

* filed herewith

21st Century Holding Company

Signatures

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

21st CENTURY HOLDING COMPANY

/s/ Edward J. Lawson

Edward J. Lawson, Chief Executive Officer and Chairman of the Board

/s/ Peter J. Prygelski, III

Peter J. Prygelski, III, Chief Financial Officer

Date: August 09, 2007

EXHIBIT INDEX

- 10.9 Indemnification Agreement between the Company and Anthony C. Kryer, III dated June 25, 2007. *
- 31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act. *
- 31.3 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act. *
- 32.2 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act. *
- 32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act. *

* filed herewith