SHACKNAI JONAH
Form 4
July 08, 2011

FORM 4

Check this box if no longer subject to Section 16. Form 4 or Form 5 obligations may continue. *See* Instruction 1(b).

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

STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

OMB APPROVAL

OMB Number:	3235-0287
Expires:	January 31, 2005
Estimated average burden hours per response...	0.5

(Print or Type Responses)

1. Name and Address of Reporting Person *
SHACKNAI JONAH
(Last) (First) (Middle)
7720 N. DOBSON RD.
(Street)
SCOTTSDALE, AZ 85256
(City) (State) (Zip)

2. Issuer Name **and** Ticker or Trading Symbol
MEDICIS PHARMACEUTICAL CORP [MRX]

3. Date of Earliest Transaction (Month/Day/Year)
06/10/2011

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer
(Check all applicable)
_____ Director _____ 10% Owner
_____ Officer (give title below) _____ Other (specify below)
CEO

6. Individual or Joint/Group Filing(Check Applicable Line)
_X_ Form filed by One Reporting Person
___ Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1.Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)		4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)			5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Indirect Beneficial Ownership (Instr. 4)
			Code	V	Amount	(A) or (D)	Price			
Common Stock	06/10/2011		G	V	123,222 (1)	D	$ 0	780,992	D	
Common Stock	07/06/2011		M (2)		276,290	A	$ 26.95	1,057,282	D	
Common Stock	07/06/2011		F		224,426	D	$ 39.7	832,856	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

number.

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned
(*e.g.*, puts, calls, warrants, options, convertible securities)

1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)		5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)		6. Date Exercisable and Expiration Date (Month/Day/Year)		7. Title and Amount o Underlying Securities (Instr. 3 and 4)	
				Code	V	(A)	(D)	Date Exercisable	Expiration Date	Title	Amoun Numbe Shares
Employee Stock Option	$ 26.95	07/06/2011		M(2)			276,290	07/17/2002	07/17/2011	Common Stock	276,2

Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
SHACKNAI JONAH 7720 N. DOBSON RD. SCOTTSDALE, AZ 85256			CEO	

Signatures

Jonah Shacknai	07/08/2011
**Signature of Reporting Person	Date

Explanation of Responses:

- * If the form is filed by more than one reporting person, *see* Instruction 4(b)(v).
- ** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. *See* 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- **(1)** Reporting person transferred 123,222 shares to an irrevocable trust for the benefit of his children.
- **(2)** The option was exercised pursuant to a Company program that permits net exercise by optionees during the last six months of the term of an option.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, *see* Instruction 6 for procedure.
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152,664,893

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As noted above, the Company's efforts to expand commercial general liability lines of insurance products are coming to fruition, as reflected by increased premiums written of $9.6 million, or 42.6 % to $32.2 million for the year ended December 31, 2006, compared to $22.6 million for the year ended December 31, 2005.

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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:

	Years Ended December 31,			
	2006		2005	
	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)			
State				
Florida	$ 22,965	71.29%	$ 18,293	80.97%
Georgia	1,805	5.60%	1,258	5.57%
Kentucky	9	0.03%	-	0.00%
Lousiania	5,743	17.83%	3,042	13.46%
South Carolina	77	0.24%	-	0.00%
Texas	1,604	4.98%	-	0.00%
Virginia	10	0.03%	-	0.00%
Total	$ 32,213	100.00%	$ 22,593	100.00%

The Company's sale of homeowners' policies increased $38.2 million, or 50.2%, to $114.4 million for the year ended December 31, 2006, as compared to $76.2 million for year ended December 31, 2005. The increase in homeowners' gross premiums written was primarily due to the Company's rate increase, with only a slight increase in the number of policy holders.

The Company's sale of auto insurance policies decreased $14.6 million, or 70.7%, to $6.1 million for the year ended December 31, 2006, as compared to $20.7 million for year ended December 31, 2005.

Gross Premiums Ceded

Gross premiums ceded increased to a debit balance of ($67.5) million for the year ended December 31, 2006, compared to a debit balance of ($31.4) million for year ended December 31, 2005. The increase was associated with the change in our prepaid reinsurance premiums in connection with our 2006-2007 hurricane season. For further discussion please see Footnote 6 titled "Reinsurance Agreements".

Increase in Prepaid Reinsurance Premiums

The increase in prepaid reinsurance premiums was $20.2 million for the year ended December 31, 2006, compared to $6.6 million for year ended December 31, 2005. The increased credit to written premium was primarily associated with the timing of our reinsurance payments measured against the term of the underling reinsurance policies.

(Increase) in Unearned Premiums

The (increase) in unearned premiums was ($16.0) million for the year ended December 31, 2006, compared to ($11.7) million for year ended December 31, 2005. The change was due to an $18.9 million increase in unearned homeowners' insurance premiums, a $4.6 million increase in unearned commercial general liability premiums, and a $7.4 million decrease in unearned automobile premiums. These changes reflect our continued growth along our homeowners' and commercial general liability lines of business. For further discussion, see "Analysis of Financial Condition - Unearned Premiums" on page 49.

Net Premiums Earned

Net premiums earned increased $6.4 million, or 7.7%, to $89.3 million for the year ended December 31, 2006, compared to $83.0 million for year ended December 31, 2005. The following table denotes net premiums earned by major product line.

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	Years Ended December 31,			
	2006		2005	
	Amount	Percentage	Amount	Percentage
Homeowners'	$ 48,206,614	53.95%	$ 40,386,025	48.68%
Commercial General Liability	27,658,007	30.96%	18,212,251	21.95%
Automobile	13,483,633	15.09%	24,365,220	29.37%
Net premiums earned	$ 89,348,254	100.00%	$ 82,963,496	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 $9.4 million, or 51.9 % to $27.7 million for the year ended December 31, 2006, compared to $18.2 million for the year ended December 31, 2005.

Finance Revenue

Finance revenue decreased $1.9 million, or 52.7%, to $1.7 million for the year ended December 31, 2006, compared to $3.6 million for year ended December 31, 2005. The decrease was primarily due to the sale in December 2004 of our assets related to our non-standard automobile insurance agency business in Florida and the finance revenue derived there from. We expect a continuing decline in finance revenue over the near future.

Managing General Agent Fees

Managing general agent fees increased $0.2 million, or 8.5%, to $2.6 million for the year ended December 31, 2006, compared to $2.4 million for year ended December 31, 2005.

Net Investment Income

Net investment income increased $2.1 million, or 54.5%, to $5.9 million for the year ended December 31, 2006, compared to $3.8 million for year ended December 31, 2005. The increase in investment income was primarily a result of the additional amounts of invested assets. Also affecting our net investment income was an increase in overall yield to 5.28% for the year ended December 31, 2006 compared to a yield of 4.66% for the year ended December 31, 2005.

Net Realized Investment Gains

Net realized investment gains increased $0.6 million, or 131.9%, to $1.1 million for the year ended December 31, 2006, compared to $0.5 million for year ended December 31, 2005. The table below depicts the gains (losses) by investment category.

	Years Ended December 31,	
	2006	2005
Realized gains:		
Fixed securities	$ 151	$ 36,981
Equity securities	1,471,307	664,162
Total realized gains	1,471,458	701,143
Realized losses:		
Fixed securities	(66,722)	(136,570)

Equity securities		(341,874)		(106,267)
Total realized losses		(408,596)		(242,837)
Net realized gains on investments	$	1,062,862	$	458,306

Other Income

Other income increased $0.6 million, or 56.5%, to $1.6 million for the year ended December 31, 2006, compared to $1.0 million for year ended December 31, 2005. Major components of other income for the year ended December 31, 2006 included $0.5 million in partial recognition of our gain on the sale of our Lauderdale Lakes property, $0.2 million in connection with a legal settlement, $0.2 million of business interruption recovery, $0.1 million in connection with FIGA fees, $0.1 million of rental income and $0.2 million of miscellaneous other sources.

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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 decreased by $3.9 million, or 8.1%, to $44.4 million for the year ended December 31, 2006, compared to $48.3 million for year ended December 31, 2005. The decrease was attributable to the increase in loss and LAE incurred during the year ended December 31, 2005 which was in connection with the adverse development associated with the 2004 hurricanes.

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 a recovery to operations of $0.1 million during the year ended December 31, 2006 from the four hurricanes that occurred in July, August, September and October of 2005.

2005 Hurricanes	Claim Count	Gross Losses	Reinsurance Recoveries	Net Losses
		(Dollars in millions)		
Dennis (July 10)	-	$ -	$ -	$ -
Katrina (August 25)	37	(0.1)	(0.1)	-
Rita (September 20)	(5)	(0.1)	-	(0.1)
Wilma (October 24)	1,517	26.0	26.0	-
Total Loss Estimate	1,549	$ 25.8	$ 25.9	$ (0.1)

The following table reflects the changes during the year ended December 31, 2006 in connection with the four hurricanes that occurred in August and September of 2004. A charge of $5.5 million occurred during the year ended December 31, 2006 in connection with these storms.

2004 Hurricanes	Claim Count	Gross Losses	Reinsurance Recoveries	Net Losses
		(Dollars in millions)		
Charley (August 13)	6	$ 3.6	$ 3.6	$ -
Frances (September 3)	4	3.2	3.1	0.1
Ivan (September 14)	(3)	4.5	-	4.5
Jeanne (September 25)	14	0.9	-	0.9

Total Loss Estimate	21	$	12.2	$	6.7	$	5.5

Our loss ratio, as determined in accordance with GAAP, for the year ended December 31, 2006 was 49.7%, compared to 58.3% for the year ended December 31, 2005. The table below reflects the loss ratios by product line.

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	Years Ended December 31,	
	2006	2005
Homeowners'	46.7%	65.5%
Commercial General Liability	38.2%	19.1%
Automobile	84.4%	75.5%
All lines	49.7%	58.3%

For further discussion, see the Note 7 to the Consolidated Financial Statements included under Part II, Item 8, of this Report.

Operating and Underwriting Expenses

Operating and underwriting expenses increased $4.9 million, or 60.1%, to $13.2 million for the year ended December 31, 2006, compared to $8.2 million for year ended December 31, 2005. The change was primarily due to a charge to operations of $3.9 million in connection with a FIGA assessment and premium tax expense which increased $1.0 million. Approvals by the OIR to recoup the assessment through an average 1.0% policy surcharge on all of our policies written in Florida over a twelve month period for new and renewal business have been granted. Premium tax expense is directly correlated to written premium, which experienced an increase in 2006.

Salaries and Wages

Salaries and wages increased $0.6 million, or 9.8%, to $7.0 million for the year ended December 31, 2006, compared to $6.4 million for year ended December 31, 2005. As a result of the adoption of SFAS 123R on January 1, 2006, salaries and wages for the year ended December 31, 2006 included a $0.5 million charge, representing approximately 85.9% of the 2006 overall increase. The remaining increase in salaries and wages was due in part to the increased labor costs in connection with additional claims loss adjusters added to our staff. We believe that salaries and wages are consistent with retaining quality management and increased premium production.

Interest Expense

Interest expense decreased $0.7 million, or 53.1%, to $0.7 million for the year ended December 31, 2006, compared to $1.4 million for year ended December 31, 2005. The change was primarily attributed to our decreased reliance upon outside sources for financing our contracts receivable.

Policy Acquisition Costs, Net of Amortization

Policy acquisition costs, net of amortization, increased $2.8 million, or 19.5%, to $17.4 million for the year ended December 31, 2006, compared to $14.6 million for year ended December 31, 2005. 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 for continuing and discontinued operations increased $2.1 million, or 39.9%, to $7.4 million for the year ended December 31, 2006, compared to $5.3 million for the year ended December 31, 2005. The effective rate for income tax expense is 34.7% for the year ended December 31, 2006, compared to 30.4% for the year ended December 31, 2005.

Net Income

As a result of the foregoing, the Company's net income for the year ended December 31, 2006 was $13.9 million compared to net income of $12.1 million for year ended December 31, 2005.

CONTRACTUAL OBLIGATIONS

A summary of long-term contractual obligations as of December 31, 2007 follows. The amounts represent estimates of gross undiscounted amounts payable over time.

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	Total	2008	2009	2010	2011	Thereafter
			(Dollars in Thousands)			
Contractual Obligations						
Unpaid Losses and LAE	$ 59,685	$ 32,827	$ 20,890	$ 5,968	$ -	$ -
Operating leases	2,524	613	625	638	648	-
Total	$ 62,209	$ 33,440	$ 21,515	$ 6,606	$ 648	$ -

LIQUIDITY AND CAPITAL RESOURCES

For the year ended December 31, 2007, our primary sources of capital were revenues generated from operations, including increased unpaid losses and LAE, decreased prepaid reinsurance premiums, increased income taxes payable, decreased premiums receivable, decreased policy acquisition costs, net of amortization, decreased premium finance contracts receivable, decreased other assets, decreased income taxes recoverable and increased bank overdrafts. Operational sources of capital also included non-cash compensation, depreciation and amortization, provision for uncollectible premiums receivable and common stock issued for interest on notes. Also contributing to our liquidity were proceeds from the sale of investment securities, exercised warrants, a tax benefit related to non-cash compensation and exercised employee stock options. Because we are a holding company, we are largely dependent upon fees and commissions from our subsidiaries for cash flow.

For the year ended December 31, 2007, operations provided net operating cash flow of $32.8 million, as compared to $27.5 million and $19.4 million for the years ended December 31, 2006 and 2005, respectively.

For the year ended December 31, 2007, operations generated $62.0 million of gross cash flow, due to a $20.1 million increase in unpaid losses and LAE, a $6.0 million decrease in prepaid reinsurance premiums, a $3.3 million increase in income taxes payable, a $4.2 million decrease in premiums receivable, a $2.2 million decrease in policy acquisition costs, net of amortization, a $1.4 million decrease in premium finance contracts receivable, a $1.2 million decrease in other assets, a $0.8 million decrease in income taxes recoverable and a $0.6 million increase in bank overdrafts. Operational sources of capital also included $0.4 million of non-cash compensation, $0.3 million of depreciation and amortization, $0.2 million in the provision for uncollectible premiums receivable and $0.1 million of common stock issued for interest on notes, all in conjunction with net income of $21.3 million.

For the year ended December 31, 2007, operations used $29.1 million of gross cash flow primarily due to a $21.4 million decrease in unearned premiums, a $2.7 million increase in reinsurance recoverable, net, a $2.0 million increase in deferred income tax expense, a $1.4 million decrease in accounts payable and accrued expenses and a $1.0 million decrease in premium deposits and customer credit balances. Additional operational uses of cash include $0.4 million of amortization of investment discount and $0.2 million of net realized investment losses.

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

For the year ended December 31, 2007, net investing activities used $19.0 million, as compared to $19.7 million and $15.5 million for the years ended December 31, 2006 and 2005, respectively. Our available for sale investment portfolio is highly liquid as it consists entirely of readily marketable securities. For the year ended December 31, 2007, investing activities generated $153.6 million and used $172.6 million from the maturity several times over of our very short municipal portfolio.

For the year ended December 31, 2007, net financing activities used $9.2 million, as compared to provided $4.1 million and used $4.0 million for the years ended December 31, 2006 and 2005, respectively. For the year ended December 31, 2007, the sources of cash in connection with financing activities included $2.0 million from the exercise of warrants, a $0.2 million tax benefit related to non-cash compensation and $0.2 million of exercised stock options. The uses of cash in connection with financing activities included $5.8 million in dividends paid, $3.8 million for the purchase of treasury stock and $2.1 million for the regularly scheduled principal and interest payments on our Notes.

We continue to 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.

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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.

Federated National's and American Vehicle's statutory capital surplus levels as of December 31, 2007 were approximately $32.3 million and $27.6 million, respectively, and their statutory net income for the year ended December 31, 2007 were $15.3 million and $1.3 million, respectively.

As of December 31, 2007, 2006, and 2005, 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.

On July 31, 2003, we completed a private placement of 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 ¾ 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.

The September 2004 Notes paid interest at the annual rate of 6%, mature on September 30, 2007, and ranked 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, 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 2004 Warrants issued to the purchasers of the September 2004 Notes and to the placement agent in the offering, J. Giordano, each entitled the holder to purchase one share of our Common Stock at an exercise price of $12.75 per share and was exercisable until September 30, 2007. The number of shares issued upon exercise of the 2004 Warrants to purchasers equaled $12.5 million divided by the exercise price of the warrants, and totaled 980,392. The number of shares issued upon exercise of the 2004 Warrants to J. Giordano equaled $500,000 divided by the exercise price of the warrants, and totaled 39,216. 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 September 2004 Warrants had zero value at the date of issuance.

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On September 30, 2007, we made the final principal payment of $1,041,667 on the September 2004 notes and the September 2004 warrants expired. Of the 1,019,608 shares that could have been issued in connection with the September 2004 warrants, 911,270 were exercised and 108,338 were unexercised. The unexercised warrants were cancelled as of September 30, 2007.

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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SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	Year Ended December 31, 2007			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(Dollars in Thousands except EPS)			
Revenue:				
Net premiums earned	$ 22,373	$ 24,814	$ 27,181	$ 24,856
Other revenue	3,212	9,679	2,390	4,627
Total revenue	25,585	34,493	29,571	29,483
Expenses:				
Losses and LAE	14,103	9,658	14,850	9,009
Other expenses	10,215	9,802	11,066	7,925
Total expenses	24,318	19,460	25,916	16,934
Income before provision for income tax expense	1,267	15,033	3,656	12,549
Provision for income tax expense	425	4,555	1,787	4,459
Net income	$ 843	$ 10,478	$ 1,869	$ 8,090
Basic net income per share	$ 0.11	$ 1.32	$ 0.24	$ 1.02
Fully diluted net income per share	$ 0.10	$ 1.31	$ 0.24	$ 1.01
Weighted average number of common shares outstanding	7,958	7,931	7,892	7,913
Weighted average number of common shares outstanding (assuming dilution)	8,187	8,015	7,948	7,988

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	Year Ended December 31, 2006			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
	(Dollars in Thousands except EPS)			
Revenue:				
Net premiums earned	$ 21,807	$ 28,741	$ 21,707	$ 17,093
Other revenue	3,307	3,601	3,063	4,595
Total revenue	25,115	32,342	24,770	21,687
Expenses:				
Losses and LAE	7,569	9,343	10,271	17,217
Other expenses	8,289	8,389	10,613	10,931
Total expenses	15,858	17,732	20,884	28,148
Income (loss) before provision (benefit) for income tax expense	9,257	14,610	3,887	(6,460)
Provision (benefit) for income tax expense	3,243	5,705	857	(2,410)
Net income (loss)	$ 6,013	$ 8,905	$ 3,029	$ (4,051)
Basic net income (loss) per share	$ 0.88	$ 1.20	$ 0.40	$ (0.52)
Fully diluted net income (loss) per share	$ 0.83	$ 1.19	$ 0.40	$ (0.52)
Weighted average number of common shares outstanding	6,845	7,428	7,561	7,846
Weighted average number of common shares outstanding (assuming dilution)	7,238	7,466	7,563	7,846

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21st Century Holding Company

OFF BALANCE SHEET TRANSACTIONS

For the years ended December 31, 2007 and 2006, there were no off balance sheet transactions.

ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

Our investment objective is to maximize total rate of return after Federal income taxes while maintaining liquidity and minimizing risk. Our current investment policy limits investment in non-investment grade fixed maturity securities (including high-yield bonds), and limits total investments in preferred stock, common stock and mortgage notes receivable. We also comply with applicable laws and regulations, which further restrict the type, quality and concentration of investments. In general, these laws and regulations permit investments, within specified limits and subject to certain qualifications, in Federal, state and municipal obligations, corporate bonds, preferred and common equity securities and real estate mortgages.

Our investment policy is established by the Board of Directors Investment Committee and is reviewed on a regular basis. Pursuant to this investment policy, as of December 31, 2007, approximately 89.4% of investments were in fixed income securities and short-term investments, which are considered to be either held until maturity or available for sale, based upon our estimates of required liquidity. Approximately 83% of the fixed maturities are considered available for sale and are marked to market. We may in the future consider additional fixed maturities to be held to maturity and carried at amortized cost. We do not use any swaps, options, futures or forward contracts to hedge or enhance our investment portfolio.

The investment portfolio is managed by the Investment Committee consisting of all current directors in accordance with guidelines established by the Florida OIR.

The table below sets forth investment results for the periods indicated.

	Years Ended December 31,		
	2007	2006	2005
	(Dollars in Thousands)		
Interest on fixed maturities	$ 6,552	$ 4,618	$ 2,970
Dividends on equity securities	565	623	660
Interest on short-term securities	691	737	209
Other	230	-	33
Total investment income	8,038	5,978	3,872
Investment expense	(74)	(45)	(31)
Net investment income	$ 7,964	$ 5,933	$ 3,841
Net realized (loss) gain	$ (145)	$ 1,063	$ 458

The following table summarizes, by type, our investments as of December 31, 2007 and 2006

	December 31, 2007		December 31, 2006	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
Fixed maturities, at market:				
	$ 61,308	45.01%	$ 97,314	77.95%

U.S. government agencies and authorities					
Obligations of states and political subdivisions		17,777	13.05%		17,804	14.26%
Corporate securities		40,609	29.81%		3,075	2.46%
Total fixed maturities		119,694	87.87%		118,193	94.67%
Equity securities, at market		16,530	12.13%		6,641	5.33%
Total investments	$	136,224	100.00%	$	124,834	100.00%

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21st Century Holding Company

Fixed maturities are carried on the balance sheet at market. At December 31, 2007 and 2006, fixed maturities had the following quality ratings by Moody's Investors Service, Inc. ("Moody's") and for securities not assigned a rating by Moody's, Standard and Poor's Company ratings were used:

	December 31, 2007		December 31, 2006	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
AAA	$ 111,795	93.40%	$ 113,353	95.91%
AA	2,819	2.36%	1,471	1.24%
A	1,889	1.58%	1,400	1.18%
BBB	2,713	2.26%	1,487	1.26%
BB++	478	0.40%	481	0.41%
Not rated	-	-	-	-
	$ 119,694	100.00%	$ 118,192	100.00%

The following table summarizes, by maturity, the fixed maturities as of December 31, 2007 and 2006.

	December 31, 2007		December 31, 2006	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
Matures In:				
One year or less	$ 29,925	25.00%	$ 17,462	14.77%
One year to five years	38,363	32.05%	80,186	67.84%
Five years to 10 years	16,400	13.70%	18,955	16.04%
More than 10 years	35,006	29.25%	1,589	1.35%
Total fixed maturities	$ 119,694	100.00%	$ 118,192	100.00%

At December 31, 2007, the weighted average maturity of the fixed maturities portfolio was approximately 5.0 years.

The following table provides information about the financial instruments as of December 31, 2007 that are sensitive to changes in interest rates. The table presents principal cash flows and the related weighted average interest rate by expected maturity date based upon par values:

	2008	2009	2010	2011	2012	Thereafter	Total	Carrying Amount
	(Dollars in Thousands)							
Principal amount by expected maturity:								
U.S. government agencies and authorities	$ 17,000	$ 400	$ 18,000	$ -	$ 8,000	$ 16,900	$ 60,300	$ 61,308
Obligations of states and political subdivisions	10,745	1,465		1,115	910	3,275	17,510	17,777
Corporate securities	2,150	500	2,400	-	500	35,148	40,698	40,609
	-	-	-	-	-	-	-	-

Collateralized mortgage obligations								
Equity securities, at market	-	-	-	-	-	-	-	16,530
Mortgage notes receivable	-	-	-	-	-	-	-	-
All investments	$ 29,895	$ 2,365	$ 20,400	$ 1,115	$ 9,410	$ 55,323	$ 118,508	$ 136,224
Weighted average interest rate by expected maturity:								
U.S. government agencies and authorities	5.15%	3.38%	5.12%	0.00%	4.38%	5.51%	5.13%	
Obligations of states and political subdivisions	4.69%	4.71%	0.00%	0.00%	3.73%	4.91%	4.38%	
Corporate securities	5.28%	7.57%	4.98%	4.17%	5.63%	5.79%	5.73%	
Collateralized mortgage obligations	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Equity securities, at market	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
Mortgage notes receivable	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	
All investments	4.99%	5.09%	5.10%	4.17%	4.38%	5.65%	5.23%	

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ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and
Stockholders of 21st Century Holding Company

We have audited the accompanying balance sheets of 21st Century Holding Company as of December 31, 2007 and 2006, and the related statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2007. We also have audited 21st Century Holding Company's internal control over financial reporting as of December 31, 2007, based on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). 21st Century Holding Company's management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Certification Report included in the Company's 2007 Form 10-K. Our responsibility is to express an opinion on these financial statements and an opinion on the company's internal control over financial reporting based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement and whether effective internal control over financial reporting was maintained in all material respects. Our audits of the financial statements included examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. Our audit of internal control over financial reporting included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audits also included performing such other procedures as we considered necessary in the circumstances. We believe that our audits provide a reasonable basis for our opinions.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of 21st Century Holding Company as of December 31, 2007 and 2006, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2007 in conformity with accounting principles generally accepted in the United States of America. Also in our opinion, 21st Century Holding Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2007, based

on criteria established in *Internal Control—Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

De Meo Young McGrath

Boca Raton, FL

March 15, 2008

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21st Century Holding Company and Subsidiaries

CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2007 AND 2006

ASSETS		2007		2006
		(Dollars in Thousands)		
Investments				
Fixed maturities, available for sale, at fair value	$	99,484	$	98,525
Fixed maturities, held to maturity, at amoritized cost		20,210		19,667
Equity securities, available for sale, at fair value		16,530		6,641
Total investments		136,224		124,834
Cash and short term investments		22,524		17,917
Receivable for investments sold		6,420		-
Finance contracts, net of allowance for credit losses of $38 in 2007 and $116 in 2006, and net of unearned finance charges of $15 in 2007 and $90 in 2006		420		1,831
Prepaid reinsurance premiums		8,471		14,460
Premiums receivable, net of allowance for credit losses of $288 and $66, respectively		3,797		7,222
Reinsurance recoverable, net		22,942		20,230
Deferred policy acquisition costs		8,958		11,153
Deferred income taxes, net		5,640		3,610
Income taxes receivable		-		787
Property, plant and equipment, net		1,046		1,296
Other assets		2,918		4,556
Total assets	$	219,361	$	207,897
LIABILITIES AND SHAREHOLDERS' EQUITY				
Unpaid losses and LAE	$	59,685	$	39,615
Unearned premiums		56,394		77,829
Premiums deposits and customer credit balances		2,761		3,793
Bank overdraft		8,695		8,107
Income taxes payable		4,226		-
Subordinated debt		-		4,167
Deferred gain from sale of property		1,998		2,467
Accounts payable and accrued expenses		4,346		5,725
Total liabilities		138,104		141,704
Commitments and Contingencies				
Shareholders' equity:				
Common stock, $0.01 par value. Authorized 37,500,000 shares; issued and outstanding 7,871,234 and 7,896,919, respectively		79		79
Additional paid-in capital		48,240		47,070

Accumulated other comprehensive (deficit)		(2,596)		(967)
Retained earnings		35,534		20,011
Total shareholders' equity		81,257		66,193
Total liabilities and shareholders' equity	$	219,361	$	207,897

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS
YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	2007	2006	2005
		(Dollars in Thousands except EPS and dividend data)	
Revenue:			
Gross premiums written	$ 133,591	$ 152,665	$ 119,440
Gross premiums ceded	(44,551)	(67,520)	(31,414)
Net premiums written	89,041	85,145	88,026
(Decrease) Increase in prepaid reinsurance premiums	(11,251)	20,193	6,623
Decrease (Increase) in unearned premiums	21,435	(15,990)	(11,686)
Net change in prepaid reinsurance premiums and unearned premiums	10,184	4,203	(5,063)
Net premiums earned	99,224	89,348	82,963
Commission income	7,214	1,679	409
Finance revenue	545	1,686	3,567
Managing general agent fees	2,035	2,625	2,420
Net investment income	7,964	5,933	3,841
Net realized investment (losses) gains	(145)	1,063	458
Other income	2,296	1,581	1,010
Total revenue	119,132	103,915	94,669
Expenses:			
Loss and LAE	47,619	44,400	48,336
Operating and underwriting expenses	12,684	13,160	8,219
Salaries and wages	6,732	7,011	6,384
Interest expense	173	656	1,398
Policy acquisition costs, net of amortization	19,420	17,395	14,561
Total expenses	86,627	82,622	78,899
Income from continuing operations before provision for income tax expense	32,505	21,293	15,771
Provision for income tax expense	11,226	7,396	4,690
Net income from continuing operations	21,280	13,896	11,081
Discontinued operations:			
Income from discontinued operations (including gain on disposal of $0, $0, and $1,630,000, respectively)	-	-	1,630

Provision for income tax expense		-		-		595
Income from discontinued operations		-		-		1,035
Net income	$	21,280	$	13,896	$	12,116
Basic net income per share from continuing operations	$	2.69	$	1.84	$	1.78
Basic net income per share from discontinued operations	$	-	$	-	$	0.17
Basic net income per share	$	2.69	$	1.84	$	1.95
Fully diluted net income per share from continuing operations	$	2.65	$	1.72	$	1.67
Fully diluted net income per share from discontinued operations	$	-	$	-	$	0.16
Fully diluted net income per share	$	2.65	$	1.72	$	1.83
Weighted average number of common shares outstanding		7,922,542		7,537,550		6,228,043
Weighted average number of common shares outstanding (assuming dilution)		8,030,205		8,085,722		6,628,076
Dividends paid per share	$	0.72	$	0.48	$	0.32

See accompanying notes to consolidated financial statements.

21st Century Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE INCOME (LOSS)
YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	Comprehensive Income	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Deficit	Retained Earnings	Treasury Stock	Total Shareholder's Equity
				(Dollars in Thousands)			
Balance as of December 31, 2004		$ 67	$ 26,310	$ (505)	$ 884	$ (1,780)	$ 24,977
Net Income	$ 12,116				$ 12,116		$ 12,116
Cash Dividends					(2,339)		(2,339)
Stock issued in lieu of cash payment for principal and interest associated with our notes		$ 2	$ 1,981				1,982
Treasury stock retired		(7)	(1,773)			$ 1,780	
Stock options exercised		4	2,816				2,819
Warrants exercised		2	2,498				2,500
Other					(255)		(255)
Net unrealized change in investments, net of tax effect of $927	(1,032)			($1,032)			(1,032)
Comprehensive income	$ 11,083						
Balance as of December 31, 2005		$ 68	$ 31,832	$ (1,537)	$ 10,405	$ -	$ 40,767
Net Income	$ 13,896				$ 13,896		$ 13,896
Cash Dividends					(4,290)		(4,290)
Stock issued in lieu of cash payment for principal and interest associated with our notes		$ 1	$ 1,794				1,795
Treasury stock		(1)	(2,000)				(2,001)
Stock options exercised		3	2,596				2,600
Warrants exercised		8	10,661				10,669
Shares based compensation			2,187				2,187
Net unrealized change in investments, net of tax effect of $344	570			$ 570			570
Comprehensive income	$ 14,466						
		$ 79	$ 47,070	$ (967)	$ 20,011	$ -	$ 66,193

Balance as of December 31, 2006							
Net Income	$ 21,280				21,280		21,280
Cash Dividends					(5,757)		(5,757)
Stock issued in lieu of cash payment for principal and interest associated with our notes		1	2,192				2,193
Treasury stock - original		(3)	(3,819)				(3,823)
Stock options exercised			176				176
Warrants exercised		2	2,033				2,035
Shares based compensation			589				589
Net unrealized change in investments, net of tax effect of $927	(1,629)			(1,629)			(1,629)
Comprehensive income	$ 19,651						-
Balance as of December 31, 2007		$ 79	$ 48,240	$ (2,596)	$ 35,534	$ -	$ 81,256

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

	2007	2006	2005
		(Dollars in Thousands)	
Cash flow from operating activities:			
Net income	$ 21,280	$ 13,896	$ 11,081
Adjustments to reconcile net income to net cash provided by operating activities:			
Amortization of investment (discount), net	(360)	(297)	(222)
Depreciation and amortization of property plant and equipment, net	317	342	445
Net realized investment (loss) gains	(188)	1,063	513
Gain on sale of assets	-	(578)	-
Common Stock issued for interest on Notes	109	128	316
(Recovery) Provision for credit losses, net	(31)	14	638
Provision (recovery) for uncollectible premiums receivable	222	(102)	(252)
Non-cash compensation	405	539	-
Changes in operating assets and liabilities:			
Premiums receivable	3,203	386	(1,229)
Prepaid reinsurance premiums	5,990	(26,793)	(6,623)
Reinsurance recoverable, net	(2,712)	140,912	(111,187)
Income taxes recoverable	787	(787)	7,915
Deferred income tax expense	(2,030)	(906)	952
Deferred gain on sale of assets	-	(2,366)	-
Policy acquisition costs, net of amortization	2,195	(1,970)	(2,226)
Premium finance contracts receivable	1,442	5,467	339
Other assets	1,169	2,491	(2,070)
Unpaid losses and LAE	20,069	(114,423)	107,468
Unearned premiums	(21,435)	15,990	11,686
Premium deposits and customer credit balances	(1,032)	1,648	273
Funds held under reinsurance treaties	-	(1,545)	1,545
Income taxes payable	4,226	(3,020)	3,020
Bank overdraft	588	(4,130)	(2,459)
Accounts payable and accrued expenses	(1,379)	1,557	841
Net cash provided by operating activities - continuing operations	32,834	27,517	20,762
Net cash (used for) operating activities - discontinued operations	-	-	(1,380)
Net cash provided by operating activities	32,834	27,517	19,381
Cash flow (used in) investing activities:			
Proceeds from sale of investment securities available for sale	195,812	271,265	122,532
Purchases of investment securities available for sale	(214,733)	(296,209)	(139,505)
Purchases of property and equipment	(67)	(400)	(182)
Proceeds from sale of assets	-	5,607	-

Net cash (used) in investing activities - continuing operations		(18,988)		(19,736)		(17,155)
Net cash provided by investing activities - discontinued operations		-		-		1,689
Net cash (used in) investing activities		(18,988)		(19,736)		(15,466)
Cash flow (used in) provided by financing activities:						
Subordinated debt (repaid)		(2,083)		(4,375)		(5,000)
Exercised stock options		177		2,600		3,059
Dividends paid		(5,758)		(4,290)		(2,339)
Exercised warrants, net		2,035		10,669		2,260
Purchase of treasury stock		(3,823)		(2,001)		-
Tax benefit related to non-cash compensation		214		(1,648)		
Revolving credit outstanding		-		(187)		(1,952)
Net cash (used in) provided by financing activities - continuing operations		(9,239)		4,064		(3,972)
Net increase (decrease) in cash and short term investments		4,608		11,845		(56)
Cash and short term investments at beginning of period		17,917		6,071		6,128
Cash and short term investments at end of period	$	22,524	$	17,917	$	6,071

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2007, 2006 AND 2005

(continued)	2007	2006	2005
Supplemental disclosure of cash flow information:			
Cash paid during the period for:			
Interest	$ 44	$ 339	$ 684
Non-cash investing and finance activities:			
Accrued dividends payable	$ 1,475	$ 1,444	$ 749
Retirement of subordinated debt by Common Stock issuance	$ 2,193	$ 1,667	$ 1,667
Stock issued to pay interest on subordinated debt	$ 109	$ 128	$ 316

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007

(1) ORGANIZATION AND BUSINESS

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

21st Century 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, personal automobile insurance and commercial automobile insurance in various states with various lines of authority through our wholly owned subsidiaries, Federated National and American Vehicle.

Insurable events during 2007 and 2006 were more normal in nature as compared to 2005 and 2004. The insurable events during 2007 and 2006 did not include any weather related catastrophic events such as the well publicized series of hurricanes that occurred in Florida during 2005 and 2004. During 2007 and 2006 we processed property and liability claims stemming from our homeowners', commercial general liability and private passenger automobile lines of business. Our automobile claims generally will exceed commercial general liability and homeowners' claims with respect to frequency of claimant activity, however the per-claim severity in connection with our commercial general liability and homeowners' lines would be expected to exceed the automobile line. Our reinsurance strategy serves to smooth the liquidity requirements imposed by the most severe insurable events and for all other insurable events we manage, at a micro and macro perspective, in the normal course of business.

We are not certain how hurricanes and other insurable events will affect our future results of operations and liquidity. Loss and LAE are affected by a number of factors including:

· the quality of the insurable risks underwritten;

· the nature and severity of the loss;

· weather-related patterns;

· the availability, cost and terms of reinsurance;

· underlying settlement costs, including medical and legal costs;

· legal and political factors such as legislative initiatives and public opinion.

We continue to manage the foregoing to the extent within our control. Many of the foregoing are partially, or entirely, outside our control.

Federated National is authorized to underwrite homeowners' property and casualty insurance in Florida as an admitted carrier.

American Vehicle is authorized as either an admitted or surplus lines carrier to underwrite commercial general liability coverage. American Vehicle has either ongoing operations or operations expected to commence this year in several states. The table below denotes by state American Vehicle's authority, status of operations and where new applications are pending. We may not receive authority to write in every state we request due to state specific

guidelines.

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21st Century Holding Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2007

States	Admitted carrier	Surplus lines carrier	Ongoing operations	Operations expected to commence this year	Application pending
Alabama	ü		ü		
Arkansas		ü		ü	
California		ü	ü		
Florida	ü		ü		
Georgia		ü	ü		
Kentucky		ü	ü		
Louisiana	ü		ü		
Maryland		ü		ü	
Missouri		ü		ü	
Nevada		ü		ü	
Ohio		ü			ü
Oklahoma		ü			ü
South Carolina		ü	ü		
Tennessee		ü			ü
Texas	ü		ü		
Virginia		ü	ü		

Additionally, both Federated National and American Vehicle are authorized to underwrite personal automobile insurance in Florida as an admitted carrier.

During 2007 American Vehicle applied for and was granted, by the State of Florida in 2008, a license to underwrite commercial multiple peril, inland marine and surety lines of business as an admitted carrier. We believe theses new lines of authority will bode well with American Vehicle’s existing customers. Operations under American Vehicle’s newly granted line of authority are expected to begin during 2008.

During the year ended December 31, 2007, 74.5%, 24.1% and 1.4% of the premiums we underwrote were for homeowners’ property and casualty insurance, commercial general liability insurance and personal automobile insurance, respectively. During the year ended December 31, 2006, 74.9%, 21.1% and 4.0% 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 insureds through our wholly owned claims adjusting company, Superior.

We are focusing our marketing efforts on continuing to expand our distribution network and market our products and services in other regions of Florida and other states by establishing relationships with additional independent agents and general agents. As this occurs, we will seek to replicate our distribution network in those states. There can be no assurance, however, that we will be able to obtain the required regulatory approvals to offer additional insurance products or expand into other states.

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 shall contract with 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 servicing additional insurance products in the future.

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(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

(a) CASH AND SHORT TERM INVESTMENTS

We consider all short-term highly liquid investments with original maturities of less than three months to be short term investments.

(b) INVESTMENTS

Our investment securities have been classified as either available-for-sale or held to maturity in response to our liquidity needs, changes in market interest rates and asset-liability management strategies, among other reasons. Investments available-for-sale are stated at fair value on the balance sheet. Investments designated as held to maturity are stated at amortized cost on the balance sheet. Unrealized gains and losses are excluded from earnings and are reported as a component of other comprehensive income within shareholders' equity, net of related deferred income taxes.

A decline in the fair value of an available-for-sale security below cost that is deemed other than temporary results in a charge to income, resulting in the establishment of a new cost basis for the security. Premiums and discounts are amortized or accreted, respectively, over the life of the related fixed maturity security as an adjustment to yield using a method that approximates the effective interest method. Dividends and interest income are recognized when earned. Realized gains and losses are included in earnings and are derived using the specific-identification method for determining the cost of securities sold.

(c) PREMIUM REVENUE

Premium revenue on all lines are earned on a pro-rata basis over the life of the policies. Unearned premiums represent the portion of the premium related to the unexpired policy term.

(d) DEFERRED ACQUISITION COSTS

Deferred acquisition costs primarily represent commissions paid to outside agents at the time of policy issuance (to the extent they are recoverable from future premium income) net of ceded premium commission earned from reinsurers, salaries and premium taxes net of policy fees, and are amortized over the life of the related policy in relation to the amount of premiums earned. The method followed in computing deferred acquisition costs limits the amount of such deferred costs to their estimated realizable value, which gives effect to the premium to be earned, related investment income, unpaid loss and LAE and certain other costs expected to be incurred as the premium is earned. There is no indication that these costs will not be fully recoverable in the near term.

(e) PREMIUM DEPOSITS

Premium deposits represent premiums received primarily in connection with homeowner policies that are not yet effective. We take approximately 30 working days to issue the policy from the date the cash and policy application are received.

(f) UNPAID LOSSES AND LAE

Unpaid losses and LAE are determined by establishing liabilities in amounts estimated to cover incurred losses and LAE. Such liabilities are determined based upon our assessment of claims pending and the development of prior years' loss liability. These amounts include liabilities based upon individual case estimates for reported losses and LAE and estimates of such amounts that are incurred but not reported. Changes in the estimated liability are charged or credited to operations as the losses and LAE are settled.

The estimates of unpaid losses and LAE are subject to the effect of trends in claims severity and frequency and are continually reviewed. As part of the process, we review historical data and consider various factors, including known and anticipated legal developments, changes in social attitudes, inflation and economic conditions. As experience develops and other data becomes available, these estimates are revised, as required, resulting in increases or decreases to the existing unpaid losses and LAE. Adjustments are reflected in results of operations in the period in which they are made and the liabilities may deviate substantially from prior estimates.

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There can be no assurance that our unpaid losses and LAE reserves will be adequate to cover actual losses. If our unpaid losses and LAE prove to be inadequate, we will be required to increase the liability with a corresponding reduction in our net income in the period in which the deficiency is identified. Future loss experience substantially in excess of the established unpaid losses and LAE could have a material adverse effect on our business, results of operations and financial condition.

Accounting for loss contingencies pursuant to SFAS 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 do not discount unpaid losses and LAE for financial statement purposes.

(g) FINANCE REVENUE

Interest and service income, resulting from the financing of insurance premiums, is recognized using a method that approximates the effective interest method. Late charges are recognized as income when chargeable.

(h) CREDIT LOSSES

Provisions for credit losses are provided in amounts sufficient to maintain the allowance for credit losses at a level considered adequate to cover anticipated losses. Generally, accounts that are over 90 days old are written off to the allowance for credit losses. We have been increasing our reliance on direct billing of our policyholders for their insurance premiums. Direct billing is when the insurance company accepts from the insured, as a receivable, a promise to pay the premium, as opposed to requiring payment of the full amount of the policy, either directly from the insured or from a premium finance company. We manage the credit risk associated with our direct billing program through our integrated computer system which allows us to monitor the equity in the unearned premium to the underlying policy. Underwriting criteria are designed with down payment requirements and monthly payments that create policyholder equity, also called unearned premium, in the insurance policy. The equity in the policy is collateral for the extension of credit to the insured.

(i) MANAGING GENERAL AGENT FEES

If substantially all the costs associated with the MGA contracts which do not involve affiliated insurers are incurred during the underwriting process, then the MGA fees and the related acquisition costs are recognized at the time the policy is underwritten, net of estimated cancellations. If the MGA contract requires significant involvement subsequent to the completion of the underwriting process, then the MGA fees and related acquisition costs are deferred and recognized over the life of the policy. Included in Managing General Agent Fees are policy fees charged by the insurance companies and passed through to Assurance MGA. Policy fees are discussed below.

(j) POLICY FEES

Policy fees represent a $25 non-refundable application fee for insurance coverage, which are intended to reimburse us for the costs incurred to underwrite the policy. The fees and related costs are recognized when the policy is underwritten. These fees are netted against underwriting costs and are included as a component of deferred acquisition costs.

(k) REINSURANCE

We recognize the income and expense on reinsurance contracts principally on a pro-rata basis over the term of the reinsurance contracts or until the reinsurers maximum liability is exhausted, whichever comes first. We are reinsured under separate reinsurance agreements for the different lines of business underwritten. Reinsurance contracts do not relieve us from our obligations to policyholders. We continually monitor our reinsurers to minimize our exposure to significant losses from reinsurer insolvencies. We only cede risks to reinsurers whom we believe to be financially sound. At December 31, 2007, all reinsurance recoverables are considered collectible.

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(l) INCOME TAXES

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the estimated future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases, and operating loss, capital loss and tax-credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income or expense in the period that includes the enactment date.

(m) CONCENTRATION OF CREDIT RISK

Financial instruments, which potentially expose us to concentrations of credit risk, consist primarily of investments, premiums receivable, amounts due from reinsurers on paid and unpaid losses and finance contracts. We have not experienced significant losses related to premiums receivable from individual policyholders or groups of policyholders in a particular industry or geographic area. We believe no credit risk beyond the amounts provided for collection losses is inherent in our premiums receivable or finance contracts. In order to reduce credit risk for amounts due from reinsurers, we seek to do business with financially sound reinsurance companies and regularly review the financial strength of all reinsurers used. Additionally, our credit risk in connection with our reinsurers is mitigated by the establishment of irrevocable clean letters of credit in favor of Federated National.

(n) RECENT ACCOUNTING PRONOUNCEMENTS

On February 15, 2007, FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities - Including an Amendment of SFAS 115.* This standard permits an entity to choose to measure many financial instruments and certain other items at fair value. This option is available to all entities, including not-for-profit organizations. Most of the provisions in Statement 159 are elective; however, the amendment to SFAS 115, *Accounting for Certain Investments in Debt and Equity Securities,* applies to all entities with available-for-sale and trading securities. FASB's stated objective in issuing this standard is as follows: "to improve financial reporting by providing entities with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions."

The fair value option established by SFAS 159 permits all entities to choose to measure eligible items at fair value at specified election dates. A business entity will report unrealized gains and losses on items for which the fair value option has been elected in earnings (or another performance indicator if the business entity does not report earnings) at each subsequent reporting date. The fair value option: (*a*) may be applied instrument by instrument, with a few exceptions, such as investments otherwise accounted for by the equity method; (*b*) is irrevocable (unless a new election date occurs); and (*c*) is applied only to entire instruments and not to portions of instruments.

SFAS 159 is effective as of the beginning of an entity’s first fiscal year that begins after November 15, 2007. Early adoption is permitted as of the beginning of the previous fiscal year provided that the entity makes that choice in the first 120 days of that fiscal year and also elects to apply the provisions of SFAS 157, *Fair Value Measurements.* 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 September 2006, FASB issued SFAS 157, "*Fair Value Measurements*", which defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. The provisions of SFAS 157 are effective for financial statements issued for fiscal years beginning after November 15, 2007, and interim periods within those fiscal years. The Company does not expect any impact upon the adoption of SFAS 157 on our consolidated financial statements.

In September 2006, FASB issued SFAS 158, "*Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans.*" This statement requires an employer to recognize the overfunded or underfunded status of a single-employer defined benefit postretirement plan as an asset or liability in its statement of financial position and to recognize changes in the funded status in the year in which the changes occur through comprehensive income. SFAS 158 is effective for years ending after December 15, 2006. There was no impact on our consolidated financial statements with respect to the adoption of SFAS 158.

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In September 2006, the SEC issued Staff Accounting Bulletin ("SAB") No. 108 to address diversity in practice in quantifying financial statement misstatements. SAB 108 requires that registrants quantify the impact on the current year's financial statements of correcting all misstatements, including the carryover and reversing effects of prior years' misstatements, as well as the effects of errors arising in the current year. SAB 108 is effective as of the first fiscal year ending after November 15, 2006, allowing a one-time transitional cumulative effect adjustment to retained earnings as of January 1, 2006, for errors that were not previously deemed material, but are material under the guidance in SAB No. 108. There was no impact on our consolidated financial statements with respect to the adoption of SAB No. 108.

In June 2006, FASB issued interpretation No. 48 ("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 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 was effective for fiscal years beginning after December 15, 2006. The Company evaluated the impact that FIN 48 will have on its Consolidated Financial Statements. Additionally, we have developed a process to capture and quantify any such effect that FIN 48 could have on the Company and concluded there was no impact on our consolidated financial statements for the year ended December 31, 2007.

In February 2006, FASB issued SFAS 155, "*Accounting for Certain Hybrid Financial Instruments*". This accounting standard permits fair value re-measurement for any hybrid financial instrument containing an embedded derivative that otherwise would require bifurcation; clarifies which interest-only strips and principal-only strips are not subject to the requirements of SFAS 133; establishes a requirement to evaluate interests in securitized financial assets to identify them as freestanding derivatives or as hybrid financial instruments containing an embedded derivative requiring bifurcation; clarifies that concentrations of credit risk in the form of subordination are not embedded derivatives; and amends SFAS 140 to eliminate the prohibition on a qualifying special-purpose entity from holding a derivative financial instrument pertaining to a beneficial interest other than another derivative financial instrument. SFAS 155 is effective for all financial instruments acquired or issued after the beginning of an entity's first fiscal year beginning after September 15, 2006. There was no impact on our consolidated financial statements with respect to the adoption of SFAS 155.

(o) USE OF ESTIMATES

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported financial statement balances as well as the disclosure of contingent assets and liabilities. Actual results could differ materially from those estimates used.

Similar to other property and casualty insurers, our liability for unpaid losses and LAE, although supported by actuarial projections and other data, is ultimately based on management's reasoned expectations of future events. Although considerable variability is inherent in these estimates, we believe that this liability is adequate. Estimates are reviewed regularly and adjusted as necessary. Such adjustments are reflected in current operations. In addition, the realization of our deferred income tax assets is dependent on generating sufficient future taxable income. It is reasonably possible that the expectations associated with these accounts could change in the near term and that the effect of such changes could be material to the Consolidated Financial Statements.

(p) OPERATIONAL RISKS

We are subject to certain risks in our business operations which are described below. Careful consideration of these risks should be made before making an investment decision. The risks and uncertainties described below are not the only ones facing 21st Century. Additional risks and uncertainties not presently known or currently deemed immaterial may also impair our business operations.

Risks Related to Our Business

- Our financial condition could be adversely affected by the occurrence of natural and man-made disasters.

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- Although we follow the industry practice of reinsuring a portion of our risks, our costs of obtaining reinsurance fluctuates and we may not be able to successfully alleviate risk through reinsurance arrangements.

- We may experience financial exposure from climate change.

- Our loss reserves may be inadequate to cover our actual liability for losses, causing our results of operations to be adversely affected.

- Our revenues and operating performance will fluctuate due to statutorily approved assessments that support property and casualty insurance pools and associations.

- Our investment portfolio may suffer reduced returns or losses, which would significantly reduce our earnings.

- We face risks in connection with potential material weakness resulting from our Sarbanes-Oxley Section 404 management report and any related remedial measures that we undertake.

- The failure of any of the loss limitation methods we employ could have a material adverse effect on our financial condition or our results of operations.

- The effects of emerging claim and coverage issues on our business are uncertain.

- Our failure to pay claims accurately could adversely affect our business, financial results and capital requirements.

- If we are unable to continue our growth because our capital must be used to pay greater than anticipated claims, our financial results may suffer.

- We may require additional capital in the future which may not be available or only available on unfavorable terms.

- Our business is heavily regulated, and changes in regulation may reduce our profitability and limit our growth.

- Our insurance companies are subject to minimum capital and surplus requirements, and our failure to meet these requirements could subject us to regulatory action.

- Our revenues and operating performance may fluctuate with business cycles in the property and casualty insurance industry.

- We may not obtain the necessary regulatory approvals to expand the types of insurance products we offer or the states in which we operate.

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

- 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.

- We rely on independent and general agents to write our insurance policies, and if we are not able to attract and retain independent and general agents, our revenues would be negatively affected.

- We rely on our information technology and telecommunications systems, and the failure of these systems could disrupt our operations.

- Nonstandard automobile insurance historically has a higher frequency of claims than standard automobile insurance, thereby increasing our potential for loss exposure beyond what we would be likely to experience if we offered only standard automobile insurance.

- Florida's personal injury protection insurance statute contains provisions that favor claimants, causing us to experience a higher frequency of claims than might otherwise be the case if we operated only outside of Florida.

- Our success depends on our ability to accurately price the risks we underwrite.

- Current operating resources are necessary to develop future new insurance products.

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- Our business strategy is to avoid competition based on price to the extent possible. This strategy, however, may result in the loss of business in the short term.

- Our senior management team is critical to the strategic direction of our company. If there were an unplanned loss of service by any of our officers our business could be harmed.

Risks Related to an Investment in Our Shares

- Our largest shareholders currently control approximately 10% of the voting power of our outstanding common stock, which could discourage potential acquirers and prevent changes in management.

- We have authorized but unissued preferred stock, which could affect rights of holders of common stock.

- Our articles of incorporation, bylaws and Florida law may discourage takeover attempts and may result in entrenchment of management.

- As a holding company, we depend on the earnings of our subsidiaries and their ability to pay management fees and dividends to the holding company as the primary source of our income.

(q) FAIR VALUE

The fair value of our investments is estimated based on prices published by financial services or quotations received from securities dealers and is reflective of the interest rate environment that existed as of the close of business on December 31, 2007 and 2006. Changes in interest rates subsequent to December 31, 2007 may affect the fair value of our investments. Refer to Note 3(a) of the Notes to Consolidated Financial Statements for details.

The carrying amounts for the following financial instrument categories approximate their fair values at December 31, 2007 and 2006 because of their short-term nature: cash and short term investments, premiums receivable, finance contracts, due from reinsurers, revolving credit outstanding, bank overdraft, accounts payable, accrued expenses and subordinated debt.

(r) STOCK OPTION PLANS

At December 31, 2007, the Company has two stock-based employee compensation plans and one stock-based franchise compensation plan, which are described later in footnote 8, Stock Compensation Plans. 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 SFAS 123, *Accounting for Stock-Based Compensation.* Under these provisions, no stock-based employee compensation cost was recognized in the Statement of Operations for the year ended December 31, 2005 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 recognitions provisions of SFAS 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized during the years ended December 31, 2007 and 2006 includes:

· Compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of Statement 123, and

· Compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair-value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated, as not required to by the pronouncement.

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(s) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is stated at cost less accumulated depreciation. Depreciation on property, plant and equipment is calculated on a straight-line basis over the following estimated useful lives: building and improvements - 30 years and furniture and fixtures - 7 years. We capitalize betterments and any other expenditure in excess of $500 if the asset is expected to have a useful life greater than one year. The carrying value of property, plant and equipment is periodically reviewed based on the expected future undiscounted operating cash flows of the related item. Based upon our most recent analysis, we believe that no impairment of property, plant and equipment exists at December 31, 2007.

(t) RECLASSIFICATIONS

Certain 2006 and 2005 financial statement amounts have been reclassified to conform to the 2007 presentations.

(3) INVESTMENTS

SFAS 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, Held-to-maturity, Trading securities or 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". We did not hold any non-traded investment securities during 2007 or 2006.

Additional provisions contained in SFAS 115 address the determination as to when an investment is considered impaired, whether that impairment is other than temporary, and the measurement of an impairment loss. The Company's policy for the valuation of temporarily impaired securities is to determine impairment based on the analysis of the following factors:

- rating downgrade or other credit event (eg., failure to pay interest when due);
- financial condition and near term prospects of the issuer, including any specific events which may influence the operations of the issuer such as changes in technology or discontinuance of a business segment;
- prospects for the issuer's industry segment;
- intent and ability of the Company to retain the investment for a period of time sufficient to allow for anticipated recovery in market value.

The fixed maturities and the equity securities that are available for sale and carried at fair value represent 85.2% of total investments as of December 31, 2007, as compared to 84.2% as of December 31, 2006. The investments held at

December 31, 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. Our equity holdings held at December 31, 2007 were primarily in trust companies, financial companies and mutual funds; and our equity holdings at December 31, 2006 were primarily in trust companies and mutual funds.

As of December 31, 2007 and 2006 we have classified $20.2 million and $19.7 million, respectively, 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 and ability to hold these securities until maturity. Additionally, we have and may continue to use this position to secure irrevocable letters of credit to facilitate business opportunities in connection with our commercial general liability program. During April 2006, American Vehicle finalized a $15.0 million irrevocable letter of credit in conjunction with the 100% Quota Share Reinsurance Agreement with Republic which was terminated in April 2007. As of December 31, 2007 the letter of credit in favor of Republic totaled $10.0 million. During January 2008 this letter of credit was reduced to $3.0 million.

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We determined that one of our securities qualified for other than temporary impairment status during the three months ended September 30, 2007. In connection with this process we charged to operations a net realized investment loss that totaled approximately $797,000, net of an estimated provisional tax effect of approximately $481,000. This investment was subsequently sold during the three months ended December 31, 2007, and we recognized an additional $200,000 loss, net of an estimated tax benefit of approximately $122,000 in connection with this security.

There were no impaired investments written down as of December 31, 2007, 2006 and 2005.

(a) FIXED MATURITIES AND EQUITY SECURITIES

The following table summarizes, by type, our investments as of December 31, 2007 and 2006.

	December 31, 2007		December 31, 2006	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
Fixed maturities, at market:				
U.S. government agencies and authorities	$ 61,308	45.01%	$ 97,314	77.95%
Obligations of states and political subdivisions	17,777	13.05%	17,804	14.26%
Corporate securities	40,609	29.81%	3,075	2.46%
Total fixed maturities	119,694	87.87%	118,193	94.67%
Equity securities, at market	16,530	12.13%	6,641	5.33%
Total investments	$ 136,224	100.00%	$ 124,834	100.00%

The following table shows the realized (losses) gains for fixed and equity securities for the years ended December 31, 2007 and 2006.

	Years Ended December 31,			
	Gains (Losses) 2007	Fair Value at Sale	Gains (Losses) 2006	Fair Value at Sale
Fixed income securities	$ 17,587	$ 28,999,444	$ 151	$ 4,000,000
Equity securities	2,115,461	27,337,819	1,471,307	62,897,114
Total realized gains	2,133,048	56,337,263	1,471,458	66,897,114
Fixed income securities	(384)	10,705,063	(66,722)	12,985,290
Equity securities	(2,278,083)	20,152,671	(341,874)	13,378,445
Total realized losses	(2,278,467)	30,857,734	(408,596)	26,363,735
Net realized (losses) gains on investments	$ (145,419)	$ 87,194,997	$ 1,062,862	$ 93,260,849

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A summary of the amortized cost, estimated fair value, gross unrealized gains and losses of fixed maturities and equity securities at December 31, 2007 and 2006 is as follows:

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
December 31, 2007				
Fixed Maturities - Available For Sale:				
U.S. government and agency obligations	$ 42,168,621	$ 56,787	$ 125,762	$ 42,099,646
Obligations of states and political subdivisions	17,277,199	67,082	68,788	17,275,493
Corporate securities	40,155,178	230,103	276,419	40,108,862
	$ 99,600,998	$ 353,972	$ 470,969	$ 99,484,001
Fixed Maturities - Held To Maturity:				
U.S. government and agency obligations	$ 19,208,295	$ 74,313	$ 88,498	$ 19,194,110
Obligations of states and political subdivisions	501,223	-	9,045	492,178
Corporate securities	500,000	2,700	11,210	491,490
	$ 20,209,518	$ 77,013	$ 108,753	$ 20,177,778
Equity securities - common stocks	$ 20,519,623	$ 18,440	$ 4,007,761	$ 16,530,302
December 31, 2006				
Fixed Maturities - Available For Sale:				
U.S. government and agency obligations	$ 79,335,392	$ 25,274	$ 713,464	$ 78,647,202
Obligations of states and political subdivisions	17,448,400	17,566	163,071	17,302,895
Corporate securities	2,660,980	6,842	92,773	2,575,049
	$ 99,444,772	$ 49,682	$ 969,308	$ 98,525,146
Fixed Maturities - Held To Maturity:				
U.S. government and agency obligations	$ 18,665,722	$ 148	$ 429,062	$ 18,236,808
Obligations of states and political subdivisions	501,483	-	7,023	494,460
Corporate securities	500,000	-	11,210	488,790
	$ 19,667,205	$ 148	$ 447,295	$ 19,220,058
Equity securities - common stocks	$ 7,272,300	$ 114,592	$ 745,592	$ 6,641,300

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The table below reflects the aging of our unrealized investment losses by investment class.

	Unrealized holdings net losses	Less than 12 months	12 months or longer
Fixed maturities:			
U.S. government obligations	$ (126,815)	$ -	$ (126,815)
Obligations of states and political subdivisions	(68,788)	-	(68,788)
	(195,603)	-	(195,603)
Corporate securities:			
Financial	(41,810)	(19,710)	(22,100)
Other	(233,556)	(72,347)	(161,209)
	(275,366)	(92,057)	(183,309)
Equity securities:			
Common stocks	(4,007,761)	(2,793,980)	(1,213,781)
Total fixed, corporate and equity securities	$ (4,478,730)	$ (2,886,037)	$ (1,592,693)

Below is a summary of fixed maturities at December 31, 2007 and 2006 by contractual or expected maturity periods. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	December 31, 2007		December 31, 2006	
	Amortized Cost	Estimated Fair Value	Amortized Cost	Estimated Fair Value
Due in one year or less	$ 30,034,570	$ 29,925,570	$ 17,467,170	$ 17,462,617
Due after one year through five years	37,218,008	38,350,186	80,448,010	80,186,000
Due after five years through ten years	16,399,262	16,412,262	19,578,795	18,955,127
Due after ten years	36,158,676	35,005,501	1,618,004	1,588,607
	$ 119,810,516	$ 119,693,519	$ 119,111,979	$ 118,192,351

United States Treasury Notes with a book value of $1,046,000, each, and maturing in 2012 were on deposit with the Florida OIR as of December 31, 2007, as required by law for both Federated National and American Vehicle and are included with other investments held until maturity.

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A summary of the sources of net investment income follows:

	Years Ended December 31,		
	2007	2006	2005
Fixed maturities	$ 6,191,238	$ 4,617,875	$ 2,969,931
Equity securities	564,634	622,791	660,309
Cash and cash equivalents	691,156	736,980	208,766
Other	591,909	-	33,000
Total investment income	8,038,937	5,977,646	3,872,006
Less investment expenses	(74,493)	(44,963)	(30,852)
Net investment income	$ 7,964,444	$ 5,932,683	$ 3,841,154

Proceeds from sales of fixed maturities and equity securities for the years ended December 31, 2007, 2006 and 2005 were approximately $202.2 million, $271.3 million and $122.5 million, respectively.

A summary of realized investment (losses) gains and (increases) in net unrealized losses follows:

	Years Ended December 31,		
	2007	2006	2005
Net realized (losses) gains:			
Fixed maturities	$ 17,203	$ (66,571)	$ (99,589)
Equity securities	(162,622)	1,129,433	557,895
Total	$ (145,419)	$ 1,062,862	$ 458,306
Net unrealized losses:			
Fixed maturities	$ (116,996)	$ (919,625)	$ (984,724)
Equity securities	(3,989,319)	(631,000)	(1,479,992)
Total	$ (4,106,315)	$ (1,550,625)	$ (2,464,716)

(4) FINANCE CONTRACTS RECEIVABLE

Below is a summary of the components of the finance contracts receivable balance:

	Years Ended December 31,	
	2007	2006
Finance contracts receivable	$ 473,240	$ 2,037,509
Less:		
Unearned income	(14,932)	(89,691)
Allowance for credit losses	(38,014)	(116,425)
Finance contracts, net of allowance for credit losses	$ 420,294	$ 1,831,393

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The activity in the allowance for credit losses was as follows:

	Years Ended December 31,	
	2007	2006
Allowance for credit losses at beginning of year	$ 116,425	$ 419,455
Recoveries credited against the allowance	(47,799)	(289,060)
Additions charged to bad debt expense	(30,612)	(13,970)
Allowance for credit losses at end of year	$ 38,014	$ 116,425

As security, Federated Premium retains a contractual right, if a premium installment is not paid when due, to cancel the insurance policy and to receive the unearned premium from the insurer.

(5) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consist of the following:

	Years Ended December 31,	
	2007	2006
Building and improvements	$ 602,000	$ 602,000
Furniture and fixtures	3,021,969	2,976,067
Property, plant and equipment, gross	3,623,969	3,578,067
Accumulated depreciation	(2,577,568)	(2,282,199)
Property, plant and equipment, net	$ 1,046,401	$ 1,295,868

Depreciation of property, plant, and equipment was $316,525, $342,108, and $444,744 during 2007, 2006 and 2005, respectively.

(6) REINSURANCE

We reinsure (cede) a portion of written premiums on an excess of loss or a quota-share basis to nonaffiliated insurance companies in order to limit our loss exposure. To the extent that reinsuring companies are unable to meet their obligations assumed under these reinsurance agreements, we remain primarily liable to our policyholders.

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The impact of the excess of loss reinsurance treaties on the financial statements is as follows:

	Years Ended December 31,		
	2007	2006	2005
Premium written:			
Direct	$ 133,591,334	$ 152,664,893	$ 119,440,297
Ceded	(44,550,721)	(67,519,911)	(31,413,815)
	$ 89,040,613	$ 85,144,982	$ 88,026,482
Premiums earned:			
Direct	$ 155,025,959	$ 137,609,238	$ 107,753,959
Ceded	(55,801,838)	(48,260,984)	(24,790,463)
	$ 99,224,121	$ 89,348,254	$ 82,963,496
Losses and LAE incurred:			
Direct	$ 71,517,245	$ 77,463,843	$ 225,350,897
Ceded	(23,898,323)	(33,063,935)	(177,014,467)
	$ 47,618,922	$ 44,399,908	$ 48,336,430

	As of December 31,	
	2007	2006
Unpaid losses and LAE, net:		
Direct	$ 59,684,790	$ 39,615,478
Ceded	(20,133,375)	(12,382,028)
	$ 39,551,416	$ 27,233,450
Unearned premiums:		
Direct	$ 56,394,473	$ 77,829,099
Ceded	(21,075,936)	(32,327,054)
	$ 35,318,537	$ 45,502,044

At December 31, 2007 prepaid reinsurance premiums were nothing, compared to $6.6 million as of December 31, 2006. These prepaid reinsurance premiums were associated with a single reinsurer and returned pursuant to provisions contained in the three-year reinsurance treaties, in which we were afforded the right to cancel the remaining two years and be entitled to receive a no loss experience commission. In connection with the cancellation of this treaty, we reported approximately $2.8 million commission income during the year ended December 31, 2007.

The Company holds collateral under related reinsurance agreements in the form of letters of credit totaling $4.1 million that can be drawn on for amounts that remain unpaid for more than 120 days.

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The impact of the quota-share reinsurance treaties on the financial statements is as follows:

	As of December 31,			
		2007		2006
Transatlantic Reinsurance Company (A+ A.M. Best Rated):				
Reinsurance recoverable on paid losses and LAE	$	20,823	$	113,061
Unpaid losses and LAE		137,546		153,114
	$	158,369	$	266,175
Amounts due from reinsurers consisted of amounts related to:				
Unpaid losses and LAE	$	137,546	$	153,114
Reinsurance recoverable on paid losses and LAE		20,823		113,061
Reinsurance receivable		-		218
	$	158,369	$	266,393

(7) UNPAID LOSSES AND LAE

The liability for unpaid losses and LAE is determined on an individual-case basis for all incidents reported. The liability also includes amounts for unallocated expenses, anticipated future claim development and IBNR.

Activity in the liability for unpaid losses and LAE is summarized as follows:

	Years Ended December 31,			
		2007		2006
Balance at January 1:	$	39,615,478	$	154,038,543
Less reinsurance recoverables		(12,382,028)		(128,419,923)
Net balance at January 1	$	27,233,450	$	25,618,620
Incurred related to:				
Current year	$	38,452,431	$	35,105,812
Prior years		9,166,491		9,294,096
Total incurred	$	47,618,922	$	44,399,908
Paid related to:				
Current year	$	15,628,017	$	17,420,147
Prior years		19,672,941		25,364,930
Total paid	$	35,300,958	$	42,785,077
Net balance at year-end	$	39,551,415	$	27,233,450
Plus reinsurance recoverables		20,133,375		12,382,028
Balance at year-end	$	59,684,790	$	39,615,478

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Based upon consultations with our independent actuarial consultants and their statement of opinion on losses and LAE, we believe that the liability for unpaid loses and LAE is adequate to cover all claims and related expenses which may arise from incidents reported.

As a result of our review of our liability for losses and LAE, which includes a re-evaluation of the adequacy of reserve levels for prior year's claims, we increased the liability for loss and LAE for claims occurring in prior years by $9,166,491, $9,294,096 and $6,094,843 for the years ended December 31, 2007, 2006 and 2005, respectively. The adjustments in the liability were primarily attributable to loss development in connection with the four hurricanes of 2004 There can be no assurance concerning future adjustments of reserves, positive or negative, for claims through December 31, 2007.

(8) REVOLVING CREDIT OUTSTANDING

Federated Premium's operations were funded by the revolving loan agreement with FlatIron. The Revolving Agreement is structured as a sale of contracts receivable under a sale and assignment agreement with WPAC, which gives them 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. There were no outstanding borrowings under the Revolving Agreement as of December 31, 2007. Outstanding borrowings under the Revolving Agreement as of December 31, 2006 and 2005 were approximately $0.01 million and $0.20 million, respectively. This credit facility terminated, at our request, during 2007.

Finance contracts receivable decreased $1.4 million, or 77.0%, to $0.4 million as of December 31, 2007, compared to $1.8 million as of December 31, 2006. We anticipate a continued decline in the short-term in connection with premiums financed contracts. The Company anticipates continued use of the direct bill feature associated with the two insurance companies and their automobile lines of business.

(9) INCOME TAXES

A summary of the provision for income tax expense is as follows:

	Years Ended December 31,		
	2007	2006	2005
Federal:			
Current	$ 10,711,544	$ 7,732,974	$ 3,710,317
Deferred	(1,247,894)	(798,161)	747,661
Provision for Federal income tax expense	9,463,650	6,934,813	4,457,978
State:			
Current	1,895,000	546,796	-
Deferred	(133,131)	(85,215)	827,244
Provision for state income tax expense	1,761,869	461,581	827,244
Provision for income tax expense	$ 11,225,519	$ 7,396,394	$ 5,285,222

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The actual income tax expense differs from the "expected" income tax expense (computed by applying the combined applicable effective federal and state tax rates to income before provision for income tax expense) as follows:

	Years Ended December 31, 2007	2006	2005
Computed expected tax provision, at federal rate	$ 11,051,807	$ 8,151,908	$ 5,211,285
State tax, net of federal deduction benefit	1,179,943	(56,242)	545,981
Tax-exempt interest	(360,397)	(304,135)	(149,627)
Dividend received deduction	(114,225)	(139,442)	(145,207)
Valuation allowance for capital loss carry forward	71,545	-	-
Interest expense not requiring cash	23,021	47,821	31,750
Other, net	(626,175)	(303,516)	(208,960)
Income tax expense, as reported	$ 11,225,519	$ 7,396,394	$ 5,285,222

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Significant components of our net deferred tax asset are as follows:

	Years Ended December 31, 2007	2006
Deferred tax assets:		
Unpaid losses and LAE	$ 1,675,398	$ 946,455
Unearned premiums	2,670,007	3,436,434
Unrealized loss on investment securities	1,510,438	583,500
Allowance for credit losses	122,819	68,693
Unearned commissions	-	183,486
Regulatory assessments	2,096,050	1,423,930
Discount on advance premiums	30,349	22,220
Unearned adjusting income	-	845
Deferred gain on sale and leaseback	607,738	838,766
Stock option expense per FASB 123 (R)	173,056	202,741
Total deferred tax assets	8,885,855	7,707,070
Deferred tax liabilities:		
Deferred acquisition costs, net	(3,331,949)	(4,157,917)
Depreciation	86,498	71,446
Prepaid expenses	(584)	(10,358)
Total deferred tax liabilities	(3,246,035)	(4,096,829)
Net deferred tax asset	$ 5,639,820	$ 3,610,241

Based upon the results of our analysis and the application of the provisions of FIN 48, we have determined that all material tax positions meet the recognition threshold and can be considered as highly certain tax positions. This is based on clear and unambiguous tax law, and we are highly confident that the full amount of each tax position will be sustained upon possible examination. Accordingly, the full amount of the tax positions will be recognized in the financial statements.

In assessing the net realizable value of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income during the periods in which those temporary differences become deductible. Management considers the scheduled reversal of deferred tax liabilities, projected future taxable income and tax planning strategies in making this assessment. At December 31, 2007 and 2006, based upon the level of historical taxable income and projections for future taxable income over the periods in which the deferred tax assets are deductible, management believes it is more likely than not that the Company will realize the benefits of these deductible differences.

The 2004, 2003 and 2002 consolidated Federal Income Tax Returns filed by the Company have been examined by the 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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(10) REGULATORY REQUIREMENTS AND RESTRICTIONS

To retain our certificate of authority, the Florida Insurance Code (the "Code") requires Federated National and American Vehicle to maintain capital and surplus equal to the greater of 10% of their liabilities or a statutory minimum capital and surplus as defined in the Code. Federated National and American Vehicle are required to have a minimum capital surplus of $4.0 million. At December 31, 2007, 2006 and 2005, Federated National's statutory capital surplus was $32.3 million, $19.5 million and $11.2 million, respectively. At December 31, 2007, 2006 and 2005, American Vehicle had statutory capital surplus of $27.6 million, $26.7 million and $18.0 million, respectively.

The insurance companies are also required to adhere to prescribed premium-to-capital surplus ratios. As of December 31, 2007, 2006 and 2005, both Federated National and American Vehicle were in compliance with the prescribed premium-to-surplus ratio.

As of December 31, 2007, to meet regulatory requirements, we had bonds with a carrying value of approximately $2.2 million pledged to the Insurance Commissioner of the State of Florida.

Under Florida law, a domestic insurer may not pay any dividend or distribute cash or other property to its shareholders except out of that part of its available and accumulated capital surplus funds which is derived from realized net operating profits on its business and net realized capital gains. A Florida domestic insurer may not make dividend payments or distributions to shareholders without prior approval of the Florida OIR if the dividend or distribution would exceed the larger of (i) the lesser of (a) 10.0% of its capital surplus or (b) net income, not including realized capital gains, plus a two-year carryforward, (ii) 10.0% of capital surplus with dividends payable constrained to unassigned funds minus 25% of unrealized capital gains or (iii) the lesser of (a) 10.0% of capital surplus or (b) net investment income plus a three-year carryforward with dividends payable constrained to unassigned funds minus 25.0% of unrealized capital gains.

Alternatively, a Florida domestic insurer may pay a dividend or distribution without the prior written approval of the Florida OIR (i) if the dividend is equal to or less than the greater of (a) 10.0% of the insurer's capital surplus as regards policyholders derived from realized net operating profits on its business and net realized capital gains or (b) the insurer's entire net operating profits and realized net capital gains derived during the immediately preceding calendar year, (ii) the insurer will have policy holder capital surplus equal to or exceeding 115.0% of the minimum required statutory capital surplus after the dividend or distribution, (iii) the insurer files a notice of the dividend or distribution with the Florida OIR at least ten business days prior to the dividend payment or distribution and (iv) the notice includes a certification by an officer of the insurer attesting that, after the payment of the dividend or distribution, the insurer will have at least 115% of required statutory capital surplus as to policyholders. Except as provided above, a Florida domiciled insurer may only pay a dividend or make a distribution (i) subject to prior approval by the Florida OIR or (ii) 30 days after the Florida OIR has received notice of such dividend or distribution and has not disapproved it within such time.

No dividends were paid by Federated National or American Vehicle in 2007, 2006 or 2005, and none are anticipated in 2008. Although we believe that amounts required to meet our financial and operating obligations will be available from sources other than dividends from our insurance subsidiaries, there can be no assurance in this regard. Further, there can be no assurance that, if requested, the Florida OIR will allow any dividends in excess of the amount available, to be paid by Federated National and American Vehicle to us in the future. The maximum dividends permitted by state law are not necessarily indicative of an insurer's actual ability to pay dividends or other distributions to a parent company, which also may be constrained by business and regulatory considerations, such as the impact of

dividends on capital surplus, which could affect an insurer's competitive position, the amount of premiums that can be written and the ability to pay future dividends. Further, state insurance laws and regulations require that the statutory capital surplus of an insurance company following any dividend or distribution by it be reasonable in relation to its outstanding liabilities and adequate for its financial needs.

In order to enhance the regulation of insurer solvency, the NAIC established risk-based capital requirements for insurance companies that are designed to assess capital adequacy and to raise the level of protection that statutory surplus provides for policy holders. These requirements measure three major areas of risk facing property and casualty insurers: (i) underwriting risks, which encompass the risk of adverse loss developments and inadequate pricing; (ii) declines in asset values arising from credit risk; and (iii) other business risks from investments. Insurers having less statutory surplus than required will be subject to varying degrees of regulatory action, depending on the level of capital inadequacy. The Florida OIR, which follows these requirements, could require Federated National or American Vehicle to cease operations in the event they fail to maintain the required statutory capital.

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Based upon the 2007 statutory financial statements for Federated National and American Vehicle, statutory surplus exceeded all regulatory action levels established by the NAIC's risk-based capital requirements. Based upon the 2006 statutory financial statements for American Vehicle, statutory surplus exceeded all regulatory action levels established by the NAIC's risk-based capital requirements. Based upon the 2006 statutory financial statements for Federated National, statutory surplus did not exceed company action levels established by the NAIC. Federated National's results required us to submit a plan containing corrective actions.

Based on Risk Based Capital requirements, the extent of regulatory intervention and action increases as the ratio of an insurer's statutory surplus to its ACL, as calculated under the NAIC's requirements, decreases. The first action level, the Company Action Level, requires an insurer to submit a plan of corrective actions to the insurance regulators if statutory surplus falls below 200.0% of the ACL amount. The second action level, the Regulatory Action Level, requires an insurer to submit a plan containing corrective actions and permits the insurance regulators to perform an examination or other analysis and issue a corrective order if statutory surplus falls below 150.0% of the ACL amount. The third action level, ACL, allows the regulators to rehabilitate or liquidate an insurer in addition to the aforementioned actions if statutory surplus falls below the ACL amount. The fourth action level is the Mandatory Control Level, which requires the regulators to rehabilitate or liquidate the insurer if statutory surplus falls below 70.0% of the ACL amount. Federated National's ratio of statutory surplus to its ACL was 653.0%, 165.4 % and 154.0% at December 31, 2007, 2006 and 2005, respectively. American Vehicle's ratio of statutory surplus to its ACL was 448.5%, 444.2% and 329.7% at December 31, 2007, 2006 and 2005, respectively.

Federated National's 2004 regularly scheduled statutory triennial examination during 2005 for the three years ended December 31, 2004 was performed by the Florida OIR. American Vehicle's examination was for the three years ended December 31, 2005 was also performed by the Florida OIR. A loss reserve deficiency totaling approximately $1.3 million (net of income taxes) was recorded in the fourth quarter of 2006 on American Vehicle in connection with this OIR examination.

We may be the subject of additional targeted examinations or analysis. These examinations or analysis may result in one or more corrective orders being issued by the Florida OIR. Federated National anticipates a regularly scheduled statutory triennial examination by the Florida OIR to occur during 2008 for the three years ended December 31, 2007 however we have not yet received any notice of such examination.

The NAIC has also developed IRIS ratios to assist state insurance departments in identifying companies which may be developing performance or solvency problems, as signaled by significant changes in the companies' operations. Such changes may not necessarily result from any problems with an insurance company, but may merely indicate changes in certain ratios outside the ranges defined as normal by the NAIC. When an insurance company has four or more ratios falling outside "usual ranges," state regulators may investigate to determine the reasons for the variance and whether corrective action is warranted.

As of December 31, 2007, Federated National was outside NAIC's usual ranges with respect to its IRIS tests on three out of thirteen ratios. There were two exceptions in connection with surplus growth and one exception in connection with adverse homeowner claims in connection with the hurricanes of 2004 and 2005.

As of December 31, 2006, Federated National was outside NAIC's usual ranges with respect to its IRIS tests on six out of thirteen ratios. There was one exception in connection with surplus growth, one exception in connection with liabilities to liquid assets and four exceptions in connection with adverse homeowner claims in connection with the 2004 hurricanes.

As of December 31, 2007, American Vehicle was outside NAIC's usual range for two of thirteen ratios. The exceptions were in connection with reserve development in connection with our Commercial General Liability program.

As of December 31, 2006, American Vehicle was outside NAIC's usual range for one of thirteen ratios. The exception was in connection with the net increase in adjusted policyholders' surplus. During 2006, net income and a decrease in non admitted securities were the major contributors to the 2006 change to policyholder surplus.

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We do not currently believe that the Florida OIR will take any significant action with respect to Federated National or American Vehicle regarding the 2007 IRIS ratios, although there can be no assurance that will be the case.

The table below reflects the range and test results for both Federated National and American Vehicle for the years ended December 31 2007 and 2006, respectively.

	Unusual Values Equal to Or		Federated National		American Vehicle	
	Over	Under	2007	2006	2007	2006
Gross Premiums to Policyholders' Surplus	900	-	312	765	122	167
Net Premium to Policyholders' Surplus	300	-	174	290	122	167
Change in Net Writings	33	-33	28	-8	-24	4
Surplus Aid to Policyholders' Surplus	15	-	-	-	-	-
Two-year Overall Operating Ratio	100	-	82	102 *	88	82
Investment Yield	6.5	3	6.2	6.4	4.9	3.9
Gross Change in Policyholders' Surplus	50.0	-10	66*	36	3	49
Net Change in Adjusted Policyholders' Surplus	25	-10	66*	36 *	3	49*
Liabilities to Liquid Assets	105	-	73	113 *	66	69
Gross Agents' Balance to Policyholders' Surplus	40	-	3	14	9	23
One-Year Reserve Development to Policyholders' Surplus	20	-	13	26 *	20 *	13
Two-Year Reserve Development to Policyholders' Surplus	20	-	49*	186 *	29 *	6
Estimated Current Reserve Deficiency to Policyholders' Surplus	25	-	19	120 *	-25	11

* indicates an unusual value

GAAP differs in some respects from reporting practices prescribed or permitted by the Florida OIR. Federated National's statutory capital and surplus was $32.3 million and $19.5 million as of December 31, 2007 and 2006, respectively. Federated National's statutory net income (loss) was $15.3 million, $1.7 million and ($2.2) million for the years ended December 31, 2007, 2006 and 2005, respectively. Federated National’s statutory non-admitted assets were approximately $1.2 million and $11.0 million as of December 31, 2007 and 2006, respectively.

American Vehicle’s statutory capital and surplus was $27.6 million and $26.7 million as of December 31, 2007 and 2006, respectively. American Vehicle’s statutory net income was approximately $1.3 million, $6.2 million and $2.9

million for the years ended December 31, 2007, 2006 and 2005 respectively. American Vehicle's statutory non-admitted assets were approximately $0.9 million and $0.4 million as of December 31, 2007 and 2006, respectively.

(11) COMMITMENTS AND CONTINGENCIES

We are involved in other 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. For additional discussion of our involvement in other claims and legal actions arising in the ordinary course of business please see ITEM 3 - LEGAL PROCEEDINGS.

The 2004, 2003 and 2002 consolidated Federal Income Tax Returns filed by the Company have been examined by the 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.

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 premium by line of business 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 association. For statutory accounting purposes these assessments are not charged to operations in contrast GAAP treatment to charge current operations for the assessments. Through policyholder surcharges, as approved by the OIR, we recouped $1.6 million in connection with these assessments during 2007. There were no assessments made for the years ended December 31, 2007 or 2005.

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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 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 $0.3 million. Provisions contained in our excess of loss reinsurance policies provide for their 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 this assessment and has recouped approximately $0.4 million and $1.2 million during 2007 and 2006, respectively. As noted above, Federated National has subrogated $1.5 million to our reinsurers.

Federated National and American Vehicle are also required to participate in an insurance apportionment plan under Florida Statutes Section 627.351, which is referred to as a 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 year ended December 31, 2007 Federated National was assessed $7,470 and American Vehicle recovered $842, by and from the JUA Plan based on its December 2007 Cash Activity Report. During the year ended December 31, 2006 Federated National and American Vehicle were assessed $221,765 and $1,579, respectively. These charges are contained in Operating and Underwriting Expenses in the Statement of Operations. Future assessments by this association are undeterminable at this time.

Bonds totaling $17.7 million secure a $10.0 million irrevocable letter of credit in order to facilitate business opportunities in connection with our commercial general liability program.

(12) LEASES

Effective on or about March 1, 2006, the Company sold its interest in the property located at 3661 West Oakland Park Boulevard, Lauderdale Lakes, Florida to an unrelated party for approximately $5.0 million cash and a $0.9 million six year 5% note. As part of the transaction, the Company agreed to lease the same facilities for a six year term; in accordance with SFAS 13, the lease will be treated as an operating lease. The expected future payout schedule is as follows:

Fiscal Year		Lease payments
2008		612,906
2009		625,165
2010		637,668
2011		648,331
Total	$	2,524,070

Rent expense for the years ended December 31, 2007, 2006 and 2005 were $0.6 million, $0.5 million and nothing, respectively.

(13) RELATED PARTY TRANSACTIONS

One of our directors is a partner at a law firm that handles some of the Company’s claims litigation. Fees paid to this law firm amounted to approximately $80,000, $258,000 and $192,000 for the years ended December 31, 2007, 2006 and 2005, respectively, and is included in LAE.

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(14) NET INCOME PER SHARE

Net income per share is computed by dividing net income by the weighted average number of shares of common stock and common stock equivalents outstanding during the periods presented.

A summary of the numerator and denominator of the basic and fully diluted 2007, 2006 and 2005 net income per share is presented below:

		Income (Loss) (Numerator)	Shares Outstanding (Denominator)		Per-share Amount
For the year ended December 31, 2007:					
Basic net income per share	$	21,279,797	7,922,542	$	2.69
Fully diluted income per share	$	21,279,797	8,030,205	$	2.65
For the year ended December 31, 2006:					
Basic net per share	$	13,896,267	7,537,550	$	1.84
Fully diluted per share	$	13,896,267	8,085,722	$	1.72
For the year ended December 31, 2005:					
Basic net (loss) per share	$	12,115,530	6,228,043	$	1.95
Fully diluted (loss) per share	$	12,115,530	6,628,076	$	1.83

(15) SEGMENT INFORMATION

SFAS 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.

If any one of the following exists, a segment must be reported on:

- 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 no segment information to report.

(16) STOCK COMPENSATION PLANS

We implemented a stock option plan in November 1998 that provides for the granting of stock options to officers, key employees and consultants. The objectives of this plan includes 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, which are either equal to or above the market value of the stock on the date of grant, typically vest over a four-year period, and expire six or 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 December 31, 2007, we had outstanding exercisable options to purchase 152,599 shares.

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In 2001, we implemented a franchisee stock option plan that provides for the granting of stock options to individuals purchasing Company owned agencies which are then converted to franchised agencies. The purpose of the plan is 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 have been granted at prices, which are 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 December 31, 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 key employees, consultants, independent contractors, 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, we are authorized to grant options to purchase up to 1,800,000 common shares, and, as of December 31, 2007, we had outstanding exercisable options to purchase 660,309 shares.

Activity in our stock option plans for the period from January 1, 2005 to December 31, 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	109,849	$	13.32	-	$	-	57,151	$	13.18
Exercised	(2,000)	$	6.67	-	$	-	(16,300)	$	10.02
Cancelled	-	$	-	-	$	-	(17,900)	$	15.82
Outstanding at December 31, 2007	152,599	$	14.92	-	$	-	660,309	$	13.78

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Options outstanding as of December 31, 2007 are exercisable as follows:

	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:									
December 31, 2007	42,750	$	14.92	-	$	-	358,506	$	13.78
December 31, 2008	21,969	$	14.92	-	$	-	101,781	$	13.78
December 31, 2009	21,970	$	14.92	-	$	-	92,129	$	13.78
December 31, 2010	21,970	$	14.92	-	$	-	69,831	$	13.78
December 31, 2011	21,970	$	14.92	-	$	-	25,631	$	13.78
Thereafter	21,970	$	14.92	-	$	-	12,431	$	13.78
Total options exercisible	152,599			-			660,309		

At December 31, 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 SFAS 123, *Accounting for Stock-Based Compensation.* Under these provisions, no stock-based employee compensation cost was recognized in the Statement of Operations for the year ended December 31, 2005 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 recognitions provisions of SFAS 123R using the modified-prospective-transition method. Under that transition method, compensation cost recognized during the years ended December 31, 2007 and 2006 includes:

- Compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of Statement 123, and

- Compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair-value estimated in accordance with the provisions of SFAS 123R. Results for prior periods have not been restated, as not required to by the pronouncement.

As a result of adopting SFAS 123R on January 1, 2006, the Company's income from continuing operations before provision for income taxes and net income for the years ended December 31, 2007 and 2006, are lower by approximately $618,000 and 405,000, and $539,000 and $336,000, 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 year ended December 31, 2007 and 2006 would have been $2.74 and 2.70, and $1.85 and $1.73, respectively, if the Company had not adopted SFAS 123R, compared to reported basic and diluted earnings per share of $2.69 and $2.65, and $1.84 and $1.72, 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 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 following table illustrates the effect on net income and earnings per share if the Company had applied the fair value recognition provisions of Statement 123 to options granted under our stock option plans in the period presented. For purposes of this provision disclosure and comparability, the value of the options were estimated using the Black-Scholes option-pricing model and amortized to expense over the options vesting periods.

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		For the Year Ended December 31, 2005
Net Income (loss) as reported	$	12,115,530
Compensation, net of tax effect		1,114,166
Pro forma net income (loss)	$	11,001,364
Net income (loss) per share		
As reported - Basic	$	1.95
As reported - Diluted	$	1.83
Pro forma - Basic	$	1.77
Pro forma - Diluted	$	1.66

The weighted average fair value of options granted during 2007, 2006 and 2005 estimated on the date of grant using the Black-Scholes option-pricing model was $2.92 to $5.59; $3.62 to $5.73 and $2.81 to $10.75, respectively.

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

	December 31, 2007	December 31, 2006	December 31, 2005
Dividend yield	3.20% to 6.70%	2.10% to 3.70%	2.33% to 2.50%
Expected volatility	42.87% to 54.77%	42.37% to 44.30%	45.51% to 96.76%
Risk-free interest rate	2.90% to 4.86%	4.60% to 4.90%	3.34% to 4.36%
Expected life (in years)	2.58 to 3.17	2.04 to 2.86	2.56 to 2.93

Summary information about the Company’s stock options outstanding at December 31, 2007

		Range of Exercise Price	Outstanding at December 31, 2007	Weighted Average Contractual Periods in Years		Weighted Average Exercise Price	Exercisable at December 31, 2007
1998 Plan	$	6.67 - $27.79	152,599	4.97	$	14.92	42,750
2001 Franchise Plan		-	-	-		-	-
2002 Plan	$	8.33 - $18.21	660,309	2.93	$	13.78	358,506

(17) EMPLOYEE BENEFIT PLAN

We have established a profit sharing plan under Section 401(k) of the Internal Revenue Code. This plan allows eligible employees, except key and highly compensated employees, to contribute up to 100 percent of their compensation on a pre-tax basis, not to exceed statutory limits. For the years ended December 31, 2007, 2006 and 2005, we did not contribute to the plan. Our contributions, if any, are vested incrementally over five years.

(18) ACQUISITIONS

We made no acquisitions during 2007.

(19) COMPREHENSIVE INCOME (LOSS)

As of December 31, 2007 and 2006 we have classified $20.2 million and $19.7 million, respectively, 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 and ability to hold these securities until maturity. Unrealized loss in connection with the 2006 reclassification totaled $0.26 million, net of a $0.16 income tax effect.

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Reclassification adjustments related to the investment securities sold and previously included in comprehensive income (loss) for the years ended December 31, 2007, 2006 and 2005 are as follows:

	Years Ended December 31,		
	2007	2006	2005
Unrealized holdings net losses arising during the year	$ (4,106,317)	$ (1,550,625)	$ (2,464,716)
Reclassification adjustment for losses included in net income	(1,550,625)	(2,464,716)	(809,639)
	(2,555,692)	914,091	(1,655,077)
Tax effect	926,939	(343,972)	622,806
Net unrealized (losses) gains on investment securities	$ (1,628,753)	$ 570,119	$ (1,032,271)

(20) AUTHORIZATION OF PREFERRED STOCK

Our Amended and Restated Articles of Incorporation authorize the issuance of one million shares of preferred stock with designations, rights and preferences determined from time to time by our board of directors. Accordingly, our board of directors is empowered, without shareholder approval, to issue preferred stock with dividends, liquidation, conversion, voting or other rights that could adversely affect the voting power or other rights of the holders of common stock. We have not issued preferred shares as of December 31, 2007.

(21) 21ST CENTURY HOLDING COMPANY

21st Century Holding Company (the parent company only) has no long term obligations, guarantees or material contingencies as of December 31, 2007. The following summarizes the major categories of the parent company's financial statements:

Condensed Balance Sheets

	Years Ended December 31,	
	2007	2006
ASSETS		
Cash and short term investments	$ 2,331,738	$ 6,337,552
Investments and advances to subsidiaries	58,744,839	58,611,395
Deferred income taxes receivable	7,552,944	787,411
Property, plant and equipment, net	518,233	550,233
Other assets	12,850,843	13,425,205
Total assets	$ 81,998,597	$ 79,711,796
LIABILITIES AND SHAREHOLDERS' EQUITY		
Subordinated debt	-	4,166,666
Income taxes payable	6,626,680	8,670,102
Dividends payable	1,474,599	1,444,316
Other liabilities	3,078,360	2,679,672

Total liabilities		11,179,639		16,960,756
Shareholders' equity:				
Common stock		80,655		86,504
Additional paid-in capital		45,310,337		45,630,368
Accumulated other comprehensive income		1,498,139		2,422,380
Retained earnings		23,929,827		14,611,788
Total shareholders' equity		70,818,958		62,751,040
Total liabilities and shareholders' equity	$	81,998,597	$	79,711,796

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Condensed Statements of Operations

	Years Ended December 31,		
	2007	2006	2005
Revenue:			
Management fees from subsidiaries	$ 1,683,378	$ 1,692,500	$ 1,655,540
Equity in income of subsidiaries	33,845,202	22,402,736	18,275,913
Net investment income	491,691	261,740	40,877
Other income	587,619	1,326,479	273,847
Total revenue	36,607,890	25,683,455	20,246,177
Expenses:			
Advertising	10,760	18,545	53,082
Salaries and wages	1,854,101	1,749,272	1,255,310
Legal fees	180,387	153,792	191,320
Interest expense and amortization of loan costs	170,948	647,698	1,322,666
Other expenses	1,886,378	1,821,487	23,047
Total expenses	4,102,574	4,390,794	2,845,425
Income before provision for income tax expense	32,505,316	21,292,661	17,400,752
Provision benefit for income tax	(11,225,519)	(7,396,394)	(5,285,222)
Net income	$ 21,279,797	$ 13,896,267	$ 12,115,530

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Condensed Statements of Cash Flow

	Years Ended December 31,		
	2007	2006	2005
Cash flow from operating activities:			
Net income	$ 21,279,797	$ 13,896,267	$ 12,115,530
Adjustments to reconcile net income to net cash (used in) provided by operating activities:			
Equity in (loss) income of subsidiaries	(33,845,202)	(22,402,736)	(11,488,883)
Depreciation and amortization of property plant and equipment, net	32,001	71,320	193,530
Common Stock issued for interest on Notes	109,375	128,125	315,625
Deferred income tax expense (benefit)	6,765,533	3,807,153	10,937,127
Income tax (payable) recoverable	(2,043,422)	(956,522)	952,098
Dividends payable	30,283	(695,475)	(306,659)
Non-cash compensation	404,800	538,775	-
Changes in operating assets and liabilities:			
Property, plant and equipment	-	2,797,968	-
Deferred gain on sale of assets	-	(2,366,101)	-
Other assets	(104,907)	1,388,004	5,852,586
Other liabilities	398,688	(2,259,029)	(6,698,263)
Net cash (used in) provided by operating activities	(6,973,054)	(6,052,251)	11,872,691
Cash flow (used in) provided by investing activities:			
Proceeds from property, plant and equipment	-	5,607,266	(2,832,770)
Purchases of investment securities available for sale	(133,444)	(4,001,960)	-
Increased capital of subsidiaries	-	-	(6,787,030)
Cash flow (used in) provided by investing activities:	(133,445)	1,605,306	(9,619,800)
Net cash (used in) provided by financing activities:			
Dividends paid	(5,757,458)	(4,289,683)	(2,339,335)
Payments against subordinated debt	(2,083,334)	(4,375,000)	(5,000,001)
Exercised warrants, net	2,034,531	10,669,372	2,259,647
Stock options exercised	176,638	2,599,558	2,819,485
Tax benefit related to non-cash compensation	213,540	1,647,751	-
Acquisition of common stock	(3,822,645)	(1,993,935)	(1,779,645)
Advances from (to) subsidiaries	12,339,412	5,991,378	(3,319,896)
Net cash (used in) provided by financing activities:	3,100,685	10,249,441	(7,359,745)
Net (decrease) increase in cash and short term investments	(4,005,814)	5,802,496	(5,106,854)
Cash and short term investments at beginning of year	6,337,552	535,056	5,641,910

Cash and short term investments at end of year	$	2,331,738	$	6,337,552	$	535,056

(22) 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.

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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 ¾ 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.

The September 2004 Notes paid interest at the annual rate of 6%, mature on September 30, 2007, and ranked 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, 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 2004 Warrants issued to the purchasers of the September 2004 Notes and to the placement agent in the offering, J. Giordano, each entitled the holder to purchase one share of our Common Stock at an exercise price of $12.75 per share and was exercisable until September 30, 2007. The number of shares issued upon exercise of the 2004 Warrants to purchasers equaled $12.5 million divided by the exercise price of the warrants, and totaled 980,392. The number of shares issued upon exercise of the 2004 Warrants to J. Giordano equaled $500,000 divided by the exercise price of the warrants, and totaled 39,216. 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 September 2004 Warrants had zero value at the date of issuance.

On September 30, 2007, we made the final principal payment of $1,041,667 on the September 2004 notes and the September 2004 warrants expired. Of the 1,019,608 shares that could have been issued in connection with the September 2004 warrants, 911,270 were exercised and 108,338 were unexercised. The unexercised warrants were cancelled as of September 30, 2007.

As indicated below, we paid, pursuant to the terms of the July 2003 Notes and in accordance with the contractual computations, selected quarterly payments of principal and interest due in shares of our Common Stock.

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Quarterly payment due date	2007	2006	2005
January 31,	n/a	-	55,537
April 30,	n/a	38,420	-
July 31,	n/a	-	-
October 31,	n/a	n/a	-
Total common stock issued	-	38,420	55,537

As indicated on the table below, 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	2005
January 31,	54,211	-	103,870
April 30,	63,114	68,696	-
July 31,	-	-	-
October 31,	n/a	-	-
Total common stock issued	117,325	68,696	103,870

For the July 2003 Notes, the quarterly principal and interest payments totaling approximately $0.6 million per payment were due quarterly with the last installment paid in cash on July 31, 2006.

For the September 2004 Notes, the quarterly principal and interest payments, totaling approximately $1.1 million per payment, were due quarterly with the last installment paid in cash on September 30, 2007.

(23) SCHEDULE VI - SUPPLEMENTAL INFORMATION CONCERNING PROPERTY-CASUALTY INSURANCE OPERATIONS

	Loss and LAE- **Current Year**	Loss and LAE- **Prior year**	Amortization of deferred policy acquisition expenses	Paid losses and LAEexpenses	Net premiums written
2007	$ 38,452,431	$ 9,166,491	$ 19,419,915	$ 15,628,017	$ 89,040,613
2006	$ 35,105,812	$ 9,294,096	$ 17,395,177	$ 17,420,147	$ 85,144,982
2005	$ 42,241,587	$ 6,094,843	$ 14,561,110	$ 25,749,109	$ 88,026,482

Affiliation with registrant	Deferred policy acquisition costs	Reserves for losses and LAE	Discount, if any, deducted from previous column	Unearned premiums	Net premiums earned	Net investment income
Consolidated Property and Casualty Subsidiaries						
2007	$ 8,958,195	$ 59,684,790	$ -	$ 56,394,473	$ 99,224,121	$ 7,964,444

2006	$	11,153,168	$	39,615,478	$	-	$	77,829,099	$	89,348,254	$ 5,932,683
2005	$	9,183,654	$	154,038,543	$	-	$	61,839,051	$	82,963,496	$ 3,841,154

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(24) DISCONTINUED OPERATIONS

On December 22, 2004 we announced our intention to sell our interest in Express Tax and EXPRESSTAX Franchise Corporation for approximately $2 million cash. This transaction closed with an effective date of January 1, 2005. The book value of Express Tax and EXPRESSTAX Franchise Corporation on January 1, 2005 was approximately $0.6 million.

Additionally, on the same day, the Company also announced a definitive agreement to sell the assets of its subsidiaries, Federated Agency Group and Fed USA, Inc., to affiliates of Affirmative Insurance Holdings, Inc. ("Affirmative")(NASDAQ: AFFM) for approximately $9.5 million. The sale of assets to Affirmative closed on December 31, 2004, at which time the Company received $7 million cash, with up to an additional $2.5 million due in the first quarter of 2006, subject to certain performance criteria being met.

Assets and liabilities, including goodwill, that were sold totaled approximately $2.1 million on December 31, 2004.

(25) SUBSEQUENT EVENTS

None

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ITEM 9 CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None

ITEM 9A CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in the reports that we file or submit under the Securities Exchange Act of 1934 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 our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

As of the end of the period covered by this report, we carried out an evaluation, under the supervision and with the participation of our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of December 31, 2007.

Management’s Report on Internal Control over Financial Reporting

Because of its inherent limitations, internal controls over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in condition, or that the degree of compliance with the policies or procedures may deteriorate.

Our management is responsible for establishing and maintaining adequate internal control over financial reporting, as such term is defined in Exchange Act Rule 13a-15(f). Under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control — Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

Based on the results of this evaluation, our management has concluded that our internal control over financial reporting was effective as of December 31, 2007 to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external reporting purposes in accordance with generally accepted accounting principles. We reviewed the results of management's assessment with the Company's Audit Committee.

Management's assessment of the effectiveness of internal control over financial reporting as of December 31, 2007 has been audited by DeMeo Young & McGrath, CPA, the independent registered public accounting firm who also audited the Company's consolidated financial statements. Their attestation report on management's assessment of the Company's internal control over financial reporting is shown on page 67.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the year ended December 31, 2007 that has materially affected, or is reasonably likely to materially affect, our internal control over financial

reporting.

Limitations on Effectiveness

Our management and our audit committee do not expect that our disclosure controls and procedures or internal control over financial reporting will prevent all errors or all instances of fraud. A control system, no matter how well designed and operated, can provide only reasonable, not absolute, assurance that the control system's objectives will be met. Further, the design of the control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provided absolute assurance that all control gaps and instances of fraud have been detected. These inherent limitations include the realities that judgments and decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. Controls can also be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is based in part upon certain assumptions about the likelihood of future events, and any design may not succeed in achieving its stated goals under all potential future conditions.

21st Century Holding Company and Subsidiaries

ITEM 9B OTHER INFORMATION

None

PART III

ITEM 10 DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Except for the information set forth under the caption "Senior Management" in Part I hereof, information required by this Item is incorporated by reference from 21st Century's definitive proxy statement, to be filed by us for our Annual Meeting of Shareholders, which meeting will involve the election of directors.

ITEM 11 EXECUTIVE COMPENSATION

Information required by this Item is incorporated by reference from our definitive proxy statement, to be filed by us for our Annual Meeting of Shareholders, which meeting will involve the election of directors.

ITEM 12 SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information required by this Item is incorporated by reference from our definitive proxy statement, to be filed by us for our Annual Meeting of Shareholders, which meeting will involve the election of directors.

ITEM 13 CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE

Information required by this Item is incorporated by reference from our definitive proxy statement, to be filed by us for our Annual Meeting of Shareholders, which meeting will involve the election of directors.

ITEM 14 PRINCIPAL ACCOUNTING FEES AND SERVICES

Information required by this Item is incorporated by reference from our definitive proxy statement, to be filed by us for our Annual Meeting of Shareholders, which meeting will involve the election of directors.

21st Century Holding Company and Subsidiaries

PART IV

ITEM 15 EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 10-K

(a) The following documents are filed as part of this report:

(1) Financial Statements

The following consolidated financial statements of the Company and the reports of independent auditors thereon are filed with this report:

Independent Auditors' Report (De Meo, Young, McGrath)

Consolidated Balance Sheets as of December 31, 2007 and 2006

Consolidated Statements of Operations for the years ended December 31, 2007, 2006 and 2005.

Consolidated Statements of Shareholders' Equity and Comprehensive Income (Loss) for the years ended December 31, 2007, 2006 and 2005.

Consolidated Statements of Cash Flows for the years ended December 31, 2007, 2006 and 2005.

Notes to Consolidated Financial Statements for the years ended December 31, 2007, 2006 and 2005.

(2) Financial Statement Schedules.

Schedule VI, Supplemental information concerning property-casualty insurance operations, is included herein under Item 8, Financial Statements and Supplementary Data.

(3) Exhibits

21st Century Holding Company and Subsidiaries

Exhibit	Description
3.1	Amended and Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 in the Company's Registration Statement on Form SB-2 filed with the SEC on September 17, 1998 [File No. 333-63623]).
3.2	Amended and Restated Bylaws of the Company (incorporated by reference to Exhibit 10.1 in the Company's Current Report on Form 8-K filed with the SEC on November 28, 2007).
4.1	Specimen of Common Stock Certificate (incorporated by reference to Exhibit 4.1 in Amendment No. 1 to the Company's Registration Statement on Form SB-2 filed with the SEC on October 7, 1998 [File No. 333-63623]).
10.1	21st Century Holding Company 2002 Stock Option Plan (incorporated by reference to Annex A in the Company's Definitive Proxy Statement for its 2002 Annual Meeting of Stockholders filed with the SEC on April 26, 2002). +
10.2	Form of 2002 Stock Option Plan Acknowledgment +
10.3	The Company's 1998 Stock Option Plan (incorporated by reference to Annex A in the Company's Definitive Proxy Statement filed with the SEC on May 12, 2000). +
10.4	Form of 1998 Stock Option Plan Acknowledgment. +
10.5	2001 Franchise Stock Option Plan (incorporated by reference to Exhibit A to the Company's Definitive Proxy Statement for its 2001 Annual Meeting of Stockholders filed with the SEC on April 30, 2001).
10.6	Form of 2001 Franchise Stock Option Plan Agreement +
10.7	Employment Agreement dated September 1, 1998 between the Company and Edward J. Lawson (incorporated by reference to Exhibit 10.2 in the Company's Registration Statement on Form SB-2 filed with the SEC on September 17, 1998 [File No. 333-63623]) +
10.8	First Modification Agreement, dated as of December 7, 2004 between the Company and Edward J. Lawson (incorporated by reference to Exhibit 10.1 in the Company's Current Report on Form 8-K dated December 7, 2004).+
10.9	Employment Agreement dated September 1, 1998 between the Company and Michele V. Lawson (incorporated by reference to Exhibit 10.3 in the Company's Registration Statement on Form SB-2 filed with the SEC on September 17, 1998 [File No. 333-63623]).+
10.10	Employment Agreement dated June 25, 2007 between the Company and Peter J. Prygelski, III (incorporated by reference to Exhibit 10.1 in the Company's Current Form 8-K filed with the SEC on June 19, 2007).+
10.11	Employment Agreement dated as of June 8, 2004 between the Company and James Gordon Jennings III (incorporated by reference to Exhibit 10.1 in the Company's Quarterly Report on Form 10-Q for the quarter ended June 30, 2004 filed with the SEC on August 16, 2004). +

10.12 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 June 19, 2007)+

10.13 Non-Compete Agreement dated December 19, 2005 between the Company and Michael Bruan dated December 19, 2005 (incorporated by reference to Exhibit 10.2 in the Company's Current Report on Form 8-K filed with the SEC on December 29, 2005).+

10.14 Non-Compete Agreement dated December 19, 2005 between the Company and J.Gordon Jennings, III (incorporated by reference to Exhibit 10.1 in the Company's Current Report on Form 8-K filed with the SEC on December 19, 2005).+

10.15 Form of Indemnification Agreement between the Company and its directors and executive officer.**

10.16 Reimbursement Contract between Federated National Insurance Company and The State Board of Administration of Florida (SBA) which administers the Florida Hurricane Catastrophe Fund (FHCF) and Addendum Nos. 1, 2, 3 and 4effective June 1, 2007 (incorporated by reference to Exhibit1 10.1 - 10.5 in the Company's Current Report on Form 8-K filed with the SEC on June 2, 2007).

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10.17	Excess Catastrophe Reinsurance Contract effective July 1, 2007 issued to Federated National Insurance Company and certain Subscribing Reinsurer(s) executing the Agreement (incorporated by reference to Exhibit 10.1 in the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007 filed with the SEC on November 9, 2007).
10.18	Reinstatement Premium Protection Reinsurance Contract effective July 1, 2007 issued to Federated National Insurance Company and certain Subscribing Reinsurance(s) executing the Agreement (incorporated by reference to Exhibit 10.2 in the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007 as filed with the SEC on November 9, 2007).
10.19	Additional Layer Excess Catastrophe Reinsurance Contract effective August 17, 2007 issued to Federated National Insurance Company and certain Subscribing Reinsurer(s) executing the Agreement (incorporated by reference to Exhibit 10.3 in the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007 filed with the SEC on November 9, 2007).
10.20	American Vehicle Insurance Company 100% Quota Share Reinsurance Agreement with Republic Underwriters Insurance Company for a portion of its business and a portion of the business assumed by it from its affiliated member companies executed on April 15, 2006 and became effective April 15, 2006 (incorporated by reference to Exhibit 10.37 in the Company's current report Form 8-K filed with the SEC on April 19, 2006).
21.1	Subsidiaries of the Company (incorporated by reference to Exhibit 21.1 in the Company's Quarterly Report on Form 10-Q for the fiscal year ended December 31, 2005 filed with the SEC on March 30, 2006).
23.1	Consent of De Meo, Young, McGrath, Independent Certified Public Accountants **
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 **

+ Management Compensation Plan or Arrangement

** Filed herewith

21st Century Holding Company and Subsidiaries

SIGNATURES

Pursuant to the requirements of Section 13 or 15 (d) of the Securities Exchange Act of 1934, the registrant has duly caused this Form 10-K report to be signed on its behalf by the undersigned, thereto duly authorized.

21st CENTURY HOLDING COMPANY

By: /s/ Edward J. Lawson

Edward J. Lawson, Chief Executive Officer
(Principal Executive Officer)

/s/ Peter J. Prygelski, III

Peter J. Prygelski, III, Chief Financial Officer
(Principal Financial Officer)

Dated: March 17, 2008

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

Signature	Title	Date
/s/ Edward J. Lawson Edward J. Lawson	Chief Executive Officer (Principal Executive Officer) Chairman of the Board	March 17, 2008
/s/ Peter J. Prygelski, III Peter J. Prygelski, III	Chief Financial Officer (Principal Financial Officer)	March 17, 2008
/s/ James G. Jennings, III James G. Jennings, III	Chief Accounting Officer	March 17, 2008
/s/ Michael H. Braun Michael H. Braun	Director	March 17, 2008
/s/ Carl Dorf Carl Dorf	Director	March 17, 2008

/s/ Bruce Simberg	Director	March 17, 2008
Bruce Simberg		
/s/ Charles B. Hart, Jr.	Director	March 17, 2008
Charles B. Hart, Jr.		
/s/ Richard W. Wilcox, Jr.	Director	March 17, 2008
Richard W. Wilcox, Jr.		
/s/ Anthony C. Krayer, III	Director	March 17, 2008
Anthony C. Krayer, III		

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EXHIBIT INDEX

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