

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2004

OR

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

FOR THE TRANSITION PERIOD FROM _____ TO _____.

Commission file number 0-2500111

21st Century Holding Company

(Exact name of registrant as specified in its charter)

<u>Florida</u>	<u>65-0248866</u>
(State or Other Jurisdiction of Incorporation or Organization)	(IRS Employer Identification No.)

3661 West Oakland Park Boulevard, Suite 300, Lauderdale Lakes, Florida 33313
(Address of principal executive offices) (Zip Code)

954-581-9993
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes [X] No []

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act).

Yes [] No [X]

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

Common Stock, \$.01 par value – 6,006,460 outstanding as of November 11, 2004.

21ST CENTURY HOLDING COMPANY

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PART I: FINANCIAL INFORMATION
ITEM 1.
FINANCIAL STATEMENTS

21ST CENTURY HOLDING COMPANY
CONSOLIDATED BALANCE SHEETS

	September 30, 2004	December 31, 2003
	<u>Unaudited</u>	<u>See Note 1</u>
ASSETS		
Investments		
Fixed maturities, available for sale, at fair value	\$ 82,696,625	\$ 43,489,598
Equity securities	6,980,404	3,663,251
Mortgage loans	-	137,571
	<hr/>	<hr/>
Total investments	89,677,029	47,290,420
Cash and cash equivalents	17,348,162	6,770,169
Receivable for investments sold	124,906	2,118,595
Finance contracts, net of allowance for credit losses of \$447,470 in 2004 and \$562,558 in 2003	7,834,719	9,891,642
Prepaid reinsurance premiums	3,080,174	8,415,095
Premiums receivable, net of allowance for credit losses of \$451,537 and \$123,000, respectively	5,843,612	7,328,256
Reinsurance recoverable, net	34,517,590	11,053,747
Deferred policy acquisition costs	7,014,774	1,739,685
Income taxes recoverable	7,202,225	824,787
Deferred income taxes	4,381,365	3,030,183
Property, plant and equipment, net	4,076,085	4,153,643
Goodwill, net	1,739,715	1,739,715
Other assets	1,821,721	2,339,656
	<hr/>	<hr/>
Total assets	\$ 184,662,077	\$ 106,695,593
LIABILITIES AND SHAREHOLDERS' EQUITY		
Unpaid losses and loss adjustment expenses	\$ 76,653,620	\$ 24,570,198
Unearned premiums	48,464,926	34,122,663
Premiums deposits	2,525,695	621,777
Revolving credit outstanding	1,281,521	4,098,786
Funds held under reinsurance treaties	9,108,429	-
Subordinated debt	17,500,000	6,875,000
Accounts payable and accrued expenses	4,441,543	4,360,793
	<hr/>	<hr/>
Total liabilities	159,975,734	74,649,217
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$0.01 par value. Authorized 37,500,000 shares; issued 6,632,209 and 6,133,386 shares, respectively; Outstanding 5,936,260 and 5,437,587, respectively	66,323	61,333
Additional paid-in capital	25,308,295	20,434,473
Accumulated other comprehensive income (deficit)	(796,272)	(324,881)
Retained earnings	1,877,968	13,643,225
Treasury stock, 695,949 shares and 695,799 shares, at cost, respectively	(1,769,971)	(1,767,774)
	<hr/>	<hr/>
Total shareholders' equity	24,686,343	32,046,376
Total liabilities and shareholders' equity	\$ 184,662,077	\$ 106,695,593

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>September 30, 2004</u>	<u>September 30, 2003</u>	<u>September 30, 2004</u>	<u>September 30, 2003</u>
Revenue:				
Gross premiums written	\$ 24,301,800	\$ 22,369,229	\$ 73,929,571	\$ 56,559,803
Gross premiums ceded	<u>71,385</u>	<u>(5,627,904)</u>	<u>975,429</u>	<u>(15,830,769)</u>
Net premiums written	<u>24,373,185</u>	<u>16,741,325</u>	<u>74,905,000</u>	<u>40,729,034</u>
Increase (decrease) in prepaid reinsurance premiums	760,823	(2,486,527)	(5,334,921)	(2,550,620)
Decrease (increase) in unearned premiums	<u>156,954</u>	<u>(2,404,301)</u>	<u>(14,342,263)</u>	<u>(4,921,972)</u>
Net change in prepaid reinsurance premiums and unearned premiums	<u>917,777</u>	<u>(4,890,828)</u>	<u>(19,677,184)</u>	<u>(7,472,592)</u>
Net premiums earned	25,290,962	11,850,497	55,227,816	33,256,442
Commission income	476,421	394,599	1,785,290	1,143,116
Finance revenue	784,584	984,644	2,824,568	3,247,673
Managing general agent fees	501,225	640,661	1,488,405	1,894,524
Net investment income	839,641	513,515	2,141,686	1,229,185
Net realized investment gains	80,959	33,765	261,386	1,453,465
Other income	<u>459,345</u>	<u>603,740</u>	<u>2,849,555</u>	<u>2,603,805</u>
Total revenue	<u>28,433,137</u>	<u>15,021,421</u>	<u>66,578,706</u>	<u>44,828,210</u>
Expenses:				
Loss and loss adjustment expenses	42,292,556	6,322,281	56,385,548	20,603,737
Operating and underwriting expenses	7,444,310	2,969,326	13,894,977	8,308,583
Salaries and wages	2,467,014	2,356,613	7,107,344	6,714,432
Interest expense	186,902	177,466	631,824	287,350
Policy acquisition costs, net of amortization	<u>2,521,738</u>	<u>123,080</u>	<u>4,645,906</u>	<u>(914,412)</u>
Total expenses	54,912,520	11,948,766	82,665,599	34,999,690
Income (loss) before provision (benefit) for income tax expense	(26,479,383)	3,072,655	(16,086,893)	9,828,520
Provision (benefit) for income tax expense	<u>(9,533,125)</u>	<u>1,081,824</u>	<u>(5,739,420)</u>	<u>3,415,354</u>
Net income (loss)	<u>\$ (16,946,258)</u>	<u>\$ 1,990,831</u>	<u>\$ (10,347,473)</u>	<u>\$ 6,413,166</u>
Basic net income (loss) per share	<u>(\$2.86)</u>	<u>\$0.42</u>	<u>(\$1.79)</u>	<u>\$1.39</u>
Weighted average number of common shares outstanding	<u>5,925,952</u>	<u>4,738,130</u>	<u>5,786,803</u>	<u>4,612,370</u>
Fully diluted net income (loss) per share	<u>(\$2.86)</u>	<u>\$0.38</u>	<u>(\$1.79)</u>	<u>\$1.32</u>
Weighted average number of common shares outstanding (assuming dilution)	<u>6,279,826</u>	<u>5,277,875</u>	<u>6,248,663</u>	<u>4,874,178</u>
Dividends declared per share	<u>\$0.08</u>	<u>\$0.07</u>	<u>\$0.16</u>	<u>\$0.17</u>

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	Nine months ended September 30,	
	2004	2003
Cash flow from operating activities:		
Net income (loss)	\$ (10,347,473)	\$ 6,413,166
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Amortization of investment premium, net	134,507	219,654
Depreciation and amortization of property plant and equipment, net	355,217	317,347
Deferred income tax expense	(1,351,182)	174,168
Net realized investment gains	80,959	(1,562,618)
Common Stock issued for interest on Notes	281,250	-
Provision for credit losses, net	707,051	470,114
Provision for uncollectible premiums receivable	(66,824)	34,627
Recognition of deferred income from sale of franchises	(131,647)	-
Changes in operating assets and liabilities:		
Premiums receivable	1,551,468	597,723
Prepaid reinsurance premiums	5,334,921	2,550,620
Due from reinsurers, net	(23,463,843)	(2,778,999)
Income taxes recoverable	(6,377,438)	-
Policy acquisition costs, net of amortization	(5,275,089)	(1,354,297)
Goodwill	-	(220,362)
Finance contracts receivable	1,349,872	(1,891,914)
Other assets	517,935	(701,574)
Unpaid losses and loss adjustment expenses	52,083,422	7,057,548
Unearned premiums	14,342,263	4,921,972
Premium deposits	1,903,918	154,371
Funds held under reinsurance treaties	9,108,429	-
Income taxes payable	-	(1,471,182)
Accounts payable and accrued expenses	80,750	(32,043)
Net cash provided by operating activities	40,818,466	12,898,321
Cash flow (used in) provided by investing activities:		
Proceeds from sale of investment securities available for sale	45,474,173	129,333,747
Purchases of investment securities available for sale	(88,685,210)	(151,221,985)
Receivable for investments sold	1,993,689	-
Collection of mortgage loans	137,571	6,247
Purchases of property and equipment	(146,012)	(576,307)
Proceeds from sale of assets	-	1,599,000
Net cash used in investing activities	(41,225,789)	(20,859,298)
Cash flow (used in) provided by financing activities:		
Subordinated debt	12,500,000	7,500,000
Exercised stock options	2,722,562	2,271,621
Dividends paid	(1,417,784)	(807,670)
Purchases of treasury stock	(2,197)	(26,667)
Revolving credit outstanding	(2,817,265)	(1,473,338)
Net cash provided by financing activities	10,985,316	7,463,946
Net (decrease) increase in cash and cash equivalents	10,577,993	(497,031)
Cash and cash equivalents at beginning of period	6,770,169	4,478,383
Cash and cash equivalents at end of period	\$ 17,348,162	\$ 3,981,352
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	\$ 160,148	\$ 156,012
Income taxes	\$ 2,095,000	\$ 4,715,000
Non-cash investing and finance activities:		
Accrued dividends payable	\$ 438,720	\$ 314,718
Retirement of subordinated debt by Common Stock issuance	\$ 1,875,000	\$ -

SEE ACCOMPANYING NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

21st Century Holding Company
Notes to Consolidated Financial Statements

(1) ORGANIZATION AND BUSINESS

The accompanying unaudited consolidated financial statements of 21st Century Holding Company (the "Company") have been prepared in accordance with generally accepted accounting principles ("GAAP") for interim financial information and with the instructions for Form 10-Q and Rule 10-01 of Regulation S-X. These financial statements do not include all information and notes required by GAAP for a complete financial statement presentation, and should be read in conjunction with the audited consolidated financial statements and notes thereto included in our annual report on Form 10-K for the year ended December 31, 2003. The December 31, 2003 year-end balance sheet data was derived from audited financial statements but does not include all disclosures required by GAAP. The financial information furnished reflects all adjustments, consisting only of normal recurring accruals, which are, in the opinion of management, necessary for a fair presentation of the financial position, results of operations and cash flows for the periods presented. The results of operations for the three-month and nine-month periods are not necessarily indicative of the results of operations that may be achieved in the future.

The accompanying consolidated financial statements include the accounts of the Company and its subsidiaries. All material intercompany accounts and transactions have been eliminated in accordance with GAAP.

We are a vertically integrated insurance holding company that, through its subsidiaries, controls substantially all aspects of the insurance underwriting, distribution and claims process. We underwrite personal automobile insurance, general liability insurance, flood insurance and homeowners' and mobile home property and casualty insurance in Florida, Louisiana and Georgia through wholly owned subsidiaries, Federated National and American Vehicle. American Vehicle has recently been authorized to write commercial general liability policies in Kentucky and expects to begin writing policies in that state in the near future. American Vehicle is a fully admitted insurance carrier in Florida and Louisiana and is admitted as a surplus lines carrier in Georgia and Kentucky.

During the nine months ended September 30, 2004, 21.4%, 63.8%, 1.6% and 13.2% of the policies we underwrote were for personal automobile insurance, homeowners' property and casualty insurance, mobile home property and casualty insurance, and commercial general liability, respectively. During the year ended December 31, 2003, 67.5%, 23.0%, 2.4% and 7.1% of the policies we underwrote were for personal automobile insurance, homeowners' property and casualty insurance, mobile home property and casualty insurance and commercial general liability, respectively. We internally process claims made by our own and third party insureds through our wholly owned claims adjusting company, Superior Adjusting, Inc. ("Superior"). We also offer premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium Finance, Inc. ("Federated Premium").

We market and distribute our own and third-party insurers' products and our other services primarily in Central and South Florida, through a network of 24 agencies owned by Federated Agency Group, Inc. ("Federated Agency Group"), a wholly owned subsidiary, 45 franchised agencies, approximately 1500 independent agents and a select number of general agents. Our independent agents and general agents are primarily responsible for the distribution of our homeowner insurance and commercial general liability products. Through our wholly owned subsidiary, FedUSA, Inc. ("FedUSA"), we franchise agencies under the FedUSA name. As of September 30, 2004, franchises were granted for 48 FedUSA agencies, of which 42 were operating and 6 are pending.

Assurance Managing General Agents, Inc., a wholly owned subsidiary, acts as Federated National's and American Vehicle's exclusive managing general agent. Assurance MGA currently provides all underwriting policy administration, marketing, accounting and financial services to Federated National, American Vehicle and our agencies, and participates in the negotiation of reinsurance contracts. Assurance MGA generates revenue through policy fee income and other administrative fees from the marketing of companies' products through the Company's distribution network. Assurance MGA plans to establish relationships with additional carriers and add additional insurance products in the future.

We offer electronic tax filing services through Express Tax Service, Inc. ("Express Tax"), an 80%-owned subsidiary, as well as franchise opportunities for these services through EXPRESSTAX Franchise Corporation. As of September 30, 2004, there were 252 franchises granted in 19 states. Revenue is generated through franchise sales, collection of royalties on tax preparation fees, incentives from business partners as well as fees from the preparation of income tax returns and income tax refund anticipation loans. In addition, Express Tax offers tax preparation services through approximately 300 licensees nationwide.

21st Century Holding Company
Notes to Consolidated Financial Statements

(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

(A) CRITICAL ACCOUNTING POLICIES

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

The most significant accounting estimates inherent in the preparation of our financial statements include estimates associated with our evaluation of the determination of liability for unpaid losses and loss adjustment expenses. In addition, significant estimates form the basis for our reserves with respect to finance contracts, premiums receivable, deferred income taxes, deferred policy acquisition costs and loss contingencies and the recoverability of goodwill. Various assumptions and other factors underlie the determination of these significant estimates. The process of determining significant estimates is fact specific and takes into account factors such as historical experience, as well as current and expected economic conditions. We periodically re-evaluate these significant factors and make adjustments where facts and circumstances dictate.

(B) IMPACT OF NEW ACCOUNTING PRONOUNCEMENTS

In January 2003, the Financial Accounting Standards Board ("FASB") issued Interpretation No. 46, Consolidation of Variable Interest Entities ("FIN 46"), which requires the consolidation of certain entities considered to be variable interest entities ("VIEs"). An entity is considered to be a VIE when it has equity investors who lack the characteristics of having a controlling financial interest, or its capital is insufficient to permit it to finance its activities without additional subordinated financial support. Consolidation of a VIE by an investor is required when it is determined that the investor will absorb a majority of the VIE's expected losses if they occur, receive a majority of the entity's expected residual returns if they occur, or both. The adoption of Interpretation No. 46 did not have any impact on our Consolidated Financial Statements.

In May 2003, the FASB issued Statement of Financial Accounting Standard Number 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This Statement establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity and it requires that an issuer classify a financial instrument that is within its scope as a liability because the financial instrument embodies an obligation of the issuer. This Statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective in the first interim period beginning after June 15, 2003. On July 31, 2003, we completed a private placement of our 6% Senior Subordinated Notes (the "July 2003 Notes"), and on September 30, 2004, we completed another private placement of our 6% Senior Subordinated Notes (the "September 2004 Notes"), both of which were offered and sold to accredited investors as units consisting of one Note with a principal amount of \$1,000 and warrants (the "Warrants") to purchase shares of our Common Stock. These Notes fall within the definition of financial instruments as described in Financial Accounting Standard Number 150 and are presented as a liability in conformity with Statement of Financial Accounting Standard Number 150. As such, the adoption of this Statement did not have any impact on our Consolidated Financial Statements.

(C) STOCK OPTIONS

We continue to account for stock-based compensation using the intrinsic value method prescribed by APB Opinion No. 25, under which no compensation cost for stock options is recognized for stock option awards granted to employees at or above fair market value. Had compensation expense for our stock compensation plans been determined based upon fair values at the grant dates for awards under the plan in accordance with SFAS No. 123, our net income and net income per share would have been reduced to the pro forma amounts indicated below.

21st Century Holding Company
Notes to Consolidated Financial Statements

	<u>For the three months ending September 30,</u>		<u>For the nine months ending September 30,</u>	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Net Income (loss) as reported	\$ (16,946,258)	\$ 1,990,831	\$ (10,347,473)	\$ 6,413,166
Compensation, net of tax effect	<u>6,171,950</u>	<u>865,096</u>	<u>6,714,508</u>	<u>1,125,656</u>
Pro forma net income	<u>\$ (23,118,208)</u>	<u>\$ 1,125,735</u>	<u>\$ (17,061,981)</u>	<u>\$ 5,287,510</u>
Net income per share				
As reported - Basic	\$ (2.86)	\$ 0.42	\$ (1.79)	\$ 1.39
As reported - Diluted	\$ (2.86)	\$ 0.38	\$ (1.79)	\$ 1.32
Pro forma - Basic	\$ (3.90)	\$ 0.24	\$ (2.95)	\$ 1.15
Pro forma - Diluted	\$ (3.90)	\$ 0.21	\$ (2.95)	\$ 1.09

Additional stock option awards are anticipated in future years.

The weighted average fair value of options granted during the nine months ended September 30, 2004, estimated on the date of grant using the Black-Scholes option-pricing model, was \$18.02. The weighted average fair value of options granted during 2004 and 2003, estimated on the date of grant using the Black-Scholes option-pricing model, was \$6.67 to \$10.74 in 2004 and \$4.21 to \$8.01 in 2003. The fair value of options granted is estimated on the date of grant using the following assumptions:

	<u>September 30, 2004</u>	<u>December 31, 2003</u>
Dividend yield	2.24% to 3.19%	1.96% to 2.10%
Expected volatility	99.65% to 103.20%	105.91% to 108.73%
Risk-free interest rate	2.13% to 3.60%	2.30% to 3.94%
Expected life (in years)	3.00 to 3.60	3.00 to 6.36

(D) EARNINGS PER SHARE

Basic earnings per share is computed by dividing net income by the weighted average number of common shares outstanding during each period presented. Diluted earnings per share is computed by dividing net income by the weighted average number of shares of common stock and common stock equivalents during the period presented; outstanding warrants and stock options are considered common stock equivalents and are included in the calculation using the treasury stock method.

On September 7, 2004, we completed a three-for-two stock split in the form of a stock dividend, whereby shareholders received three shares of common stock for every two shares of our common stock held on the record date. Just prior to the three-for-two stock split, we had approximately 3,957,000 shares outstanding, and following the stock split, we had approximately 5,936,000 shares outstanding, including fractional shares that were paid in common stock. All earnings per share data included in the consolidated financial statements and notes thereto has been restated after giving retroactive effect for the September 7, 2004 three-for-two stock split.

(E) RECLASSIFICATIONS

Certain amounts in 2003 financial statements have been reclassified to conform to the 2004 presentation.

(3) REVOLVING CREDIT OUTSTANDING

Federated Premium's operations are funded by a revolving loan agreement ("Revolving Agreement") with FlatIron Funding Company LLC ("FlatIron"). The Revolving Agreement is structured as a sale of contracts receivable under a sale and assignment agreement with FPF, Inc. ("FPF", a wholly-owned subsidiary of FlatIron), which gives FPF 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.

During September 2004, we negotiated a new revolving loan agreement with FPF in which the maximum credit commitment available to us was reduced at our request to \$2.0 million with built-in options to incrementally increase the maximum credit commitment up \$4.0 million over the next three years. We believe that this available

21st Century Holding Company
Notes to Consolidated Financial Statements

credit is sufficient based on our current operations. Our lender, however, could decide to reduce our available credit based on a number of factors, including the A.M. Best ratings of Federated National and American Vehicle. If the A.M. Best rating of Federated National falls below a "C", or if the financial condition of American Vehicle, as determined by our lender (in its sole and absolute discretion) suffers a material adverse change, then under the terms of our revolving loan agreement, policies written by that subsidiary will no longer be eligible collateral, causing our available credit to be reduced. If that occurs and we are not able to obtain working capital from other sources, then we would have to restrict our growth and, possibly, our operations.

The amount of FPF's advance is subject to availability under a borrowing base calculation, with maximum advances outstanding not to exceed the credit commitment. The annual interest rate on advances under the Revolving Agreement is the prime rate plus additional interest varying from 1.25% to 3.25% based on the prior month's ratio of contracts receivable related to insurance companies with an A. M. Best rating of B or lower to total contracts receivable. As of September 30, 2004, our rate was 4.75% as compared to our rate as of September 30, 2003 of 5.75%.

The Revolving Agreement contains various operating and financial covenants, with which we were in compliance at September 30, 2004 and December 31, 2003. Outstanding borrowings under the Revolving Agreement as of September 30, 2004 and December 31, 2003 were \$1.3 million and \$4.1 million, respectively. Outstanding borrowings in excess of the \$4.0 million commitment totaled \$98,786 as of December 31, 2003. The excess amount, permissible by reason of a compensating cash balance of \$200,430 for December 31, 2003, was held for the benefit of FPF and is included in other assets. Interest expense on this revolving credit line for the nine months ended September 30, 2004 and 2003 totaled approximately \$150,000 and \$156,000, respectively. For the nine months ended September 30, 2004 and 2003 the effective interest rate on this line of credit, based on our average outstanding borrowings under the Revolving Agreement, was 6.97% and 5.90%, respectively.

(4) COMMITMENTS AND CONTINGENCIES

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

In June 2000, a lawsuit was filed against us, our directors and our executive officers seeking compensatory damages in an undisclosed amount on the basis of allegations that our amended registration statement dated November 4, 1998 was inaccurate and misleading concerning the manner in which we recognized ceded insurance commission income, in violation of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. The lawsuit was filed in the United States District Court for the Southern District of New York. The plaintiff class purportedly includes purchasers of our Common Stock between November 5, 1998 and August 13, 1999. The Court granted the plaintiffs class status.

Specifically, the plaintiffs allege that we recognized ceded commission income on a written basis, rather than amortized on a pro rata basis. The plaintiffs allege that this was contrary to the Statement of Financial Accounting Concepts Nos. 1, 2 and 5. We believe, however, that the lawsuit is without merit and we have vigorously defended the action, because we reasonably relied upon outside subject matter experts to make these determinations at the time. We have also since accounted for ceded commission on a pro rata basis and have done so since these matters were brought to our attention in 1998. Nevertheless, we have also continued to actively participate in settlement negotiations with the plaintiffs and have tentatively agreed to settle the case. The parties are currently negotiating the final terms of a Memorandum of Understanding, which will have to be executed by the parties and then approved by the court. We have reserved and charged against fourth quarter 2003 earnings \$600,000 for the potential settlement and associated costs.

As a direct premium writer in the State of Florida, we are required to participate in certain insurer solvency pools under Florida Statutes section 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.

Federated National and American Vehicle are also required to participate in an insurance apportionment plan under Florida Statutes section 627.351 referred to as a Joint Underwriting Association Plan ("JUA Plan"). The JUA Plan provides for the equitable apportionment of any profits realized, or losses and expenses incurred, among

21st Century Holding Company
Notes to Consolidated Financial Statements

participating insurers. In the event of an underwriting deficit incurred by the JUA Plan and the deficit 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 premiums of each such member written during the preceding calendar year bear to the aggregate net direct premiums written in this state by all members of the JUA Plan.

On September 28, 2004, Federated National and American Vehicle were assessed by the JUA Plan \$362,121 and \$120,009, respectively. These assessments were charged against current operations. Future assessments against either insurance company are not reasonably predictable in terms of frequency or amounts.

(5) COMPREHENSIVE INCOME

For the three and nine months ended September 30, 2004 and 2003, comprehensive income consisted of the following:

	Three months ended September 30,		Nine months ended September 30,	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Net income	\$ (16,946,258)	\$ 1,990,831	\$ (10,347,473)	\$ 6,413,166
Change in net unrealized gains on investments available for sale	<u>1,772,140</u>	<u>82,369</u>	<u>(169,579)</u>	<u>241,830</u>
Comprehensive income, before tax	(15,174,118)	2,073,200	(10,517,052)	6,654,996
Income tax benefit (expense) related to items of other comprehensive income	<u>(661,633)</u>	<u>(32,537)</u>	<u>69,036</u>	<u>(95,524)</u>
Comprehensive income	<u>\$ (15,835,751)</u>	<u>\$ 2,040,663</u>	<u>\$ (10,448,016)</u>	<u>\$ 6,559,472</u>

(6) SEGMENT INFORMATION

We operate principally in two business segments consisting of insurance and financing. The insurance segment consists of underwriting through Federated National and American Vehicle, managing general agent operations through Assurance MGA, claims processing through Superior, and marketing and distribution through Federated Agency Group. The insurance segment sells personal automobile, general liability, homeowner's and mobile homeowner's insurance and includes substantially all aspects of the insurance, distribution and claims process. The financing segment consists of premium financing through Federated Premium. The financing segment provides premium financing to our insureds and is marketed through our distribution network of Company-owned agencies and franchised agents.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies and practices. We evaluate our business segments based on GAAP pretax operating earnings. Corporate overhead expenses are allocated to business segments. Transactions between reportable segments are accounted for at fair value.

Operating segments that are not individually reportable, based on the extent of the current operations in such segments, are included in the "All Other" category. The "All Other" category currently includes the operations of 21st Century Holding Company, franchise operations and income tax preparation.

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Information regarding components of operations for the three and nine months ended September 30, 2004 and 2003 follows:

	<u>Three months ended September 30,</u>		<u>Nine months ended September 30,</u>	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Total revenue				
Insurance segments	\$ 29,131,025	\$ 16,991,819	\$ 66,547,303	\$ 46,705,850
Financing segment	594,540	598,290	2,118,732	1,878,531
All other segments	<u>915,812</u>	<u>349,660</u>	<u>4,122,925</u>	<u>3,840,782</u>
Total operating segments	30,641,377	17,939,769	72,788,960	52,425,163
Intercompany eliminations	<u>(2,208,240)</u>	<u>(2,918,348)</u>	<u>(6,210,254)</u>	<u>(7,596,953)</u>
Total revenues	<u>\$ 28,433,137</u>	<u>\$ 15,021,421</u>	<u>\$ 66,578,706</u>	<u>\$ 44,828,210</u>
Earnings before income taxes				
Insurance segments	\$ (26,594,817)	\$ 2,990,072	\$ (17,374,061)	\$ 8,173,155
Financing segment	213,266	243,538	800,027	514,387
All other segments	<u>(97,832)</u>	<u>(160,955)</u>	<u>487,141</u>	<u>1,140,978</u>
Total earnings before income taxes	<u>\$ (26,479,383)</u>	<u>\$ 3,072,655</u>	<u>\$ (16,086,893)</u>	<u>\$ 9,828,520</u>

Information regarding total assets as of September 30, 2004 and December 31, 2003 follows:

	<u>September 30, 2004</u>	<u>December 31, 2003</u>
Total assets		
Insurance segments	\$ 171,031,140	\$ 93,301,125
Financing segment	7,979,364	10,105,548
All other segments	<u>18,719,496</u>	<u>3,602,606</u>
Total operating segments	197,730,000	107,009,279
Intercompany eliminations	<u>(13,067,923)</u>	<u>(313,686)</u>
Total assets	<u>\$ 184,662,077</u>	<u>\$ 106,695,593</u>

(7) REINSURANCE AGREEMENTS

We are not subscribing to quota-share reinsurance for automobile insurance policies issued with an effective date beyond December 31, 2003. The quota-share reinsurance treaties for 2003 automobile insurance policies include loss corridors with varying layers of coverage based on ultimate incurred loss ratio results whereby Federated National and American Vehicle will retain 100% of the losses between incurred loss ratios of 66% and 86%. Despite the loss corridors, substantially all of the insurance risk relating to the reinsured portions of the underlying insurance agreements has been assumed by the reinsurer, wherein the reinsurer's exposure to loss is essentially the same as ours.

We continue to participate in the Florida Hurricane Catastrophe Fund ("FCAT") and we subscribe to an excess of loss reinsurance policy to protect our interest in the insurable risks associated with our homeowner and mobile home owner insurance products. Maximum coverage afforded from the combined policies of our FCAT and excess of loss policies in effect for varying dates from June 1, 2004 to June 30, 2005 total approximately \$200.0 million where we will retain the first \$10 million of insurable losses on each event. Our amount of reinsurance coverage was determined by subjecting our homeowner and mobile homeowner exposures to statistical forecasting models that are designed to quantify a catastrophic event in terms of the frequency of a storm occurring once in every "n" years. Our reinsurance coverage contemplated a catastrophic event occurring once every 100 years. As a result of the hurricanes experienced in Florida in August and September 2004, we incurred a net reinstatement insurance premium of \$3.0 million that is amortized through operations from the reinstatement date of August 13, 2004 to June 30, 2005.

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(8) STOCK COMPENSATION PLANS

In 1998, we issued warrants to two employees to purchase a total of 62,500 shares of our common stock at \$9.00 per share. The warrants vested immediately and are exercisable until December 2004, at which time if they have not been exercised, they will be canceled. The estimated fair value of these warrants at the date issued was approximately \$226,000 using a Black-Scholes option pricing model and assumptions similar to those used for valuing the Company's stock options as described below. During the nine months ended September 30, 2004, all of the 7,800 remaining warrants were exercised.

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 include attracting and retaining the best personnel, providing for additional performance incentives, and promoting our success by providing employees the opportunity to acquire common stock. Options outstanding under this plan have been granted at prices that are either equal to or above the market value of the stock on the date of grant, vest over a four-year period, and expire ten years after the grant date. Under this plan, we are authorized to grant options to purchase up to 900,000 common shares, and, as of September 30, 2004 and December 31, 2003, we had outstanding exercisable options to purchase 239,158 and 408,530 shares, respectively.

In 2001, we implemented a franchisee stock option plan that provides for the granting of stock options to individuals purchasing Company-owned agencies that 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 that 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 1,033,500 common shares, and as of September 30, 2004 and December 31, 2003, we had outstanding exercisable options to purchase 15,000 and 39,960 shares, respectively.

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 thereunder, 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 that 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 September 30, 2004 and December 31, 2003, we had outstanding exercisable options to purchase 906,900 and 938,100 shares, respectively.

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Activity in the Company's stock option plans for the period from January 1, 2002 to September 30, 2004 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 December 31, 2001	618,858	\$ 6.67	125,745	\$ 6.67	-	
Granted	342,398	\$ 6.67			1,174,500	\$ 8.91
Exercised	(1,500)				-	
Cancelled	(158,249)	\$ 6.67	(8,512)	\$ 6.67	(84,000)	\$ 9.02
Outstanding at December 31, 2002	801,507	\$ 6.67	117,233	\$ 6.67	1,090,500	\$ 8.90
Granted	-	\$ 6.67	15,000	\$ 9.17	152,250	\$ 10.51
Exercised	(375,371)	\$ 6.67	(92,273)	\$ 6.67	(216,900)	\$ 8.57
Cancelled	(17,606)	\$ 6.67	-		(87,750)	\$ 9.37
Outstanding at December 31, 2003	408,530	\$ 6.67	39,960	\$ 7.61	938,100	\$ 9.20
Granted	-		-		168,750	\$ 18.02
Exercised	(155,872)	\$ 6.67	(24,960)	\$ 6.67	(130,800)	\$ 9.16
Cancelled	(13,500)	\$ 6.67	-		(69,150)	\$ 10.59
Outstanding at September 30, 2004	239,158	\$ 6.67	15,000	\$ 9.17	906,900	\$ 10.74

Options outstanding as of September 30, 2004 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:						
September 30, 2004	143,907	\$ 6.67	15,000	\$ 6.67	411,126	\$ 8.90
December 31, 2004	-	\$ 6.67	-	\$ 6.67	18,300	\$ 8.90
December 31, 2005	47,625	\$ 6.67	-	\$ 6.67	136,608	\$ 8.90
December 31, 2006	47,626	\$ 6.67	-	\$ 6.67	136,608	\$ 8.90
December 31, 2007	-	\$ -	-	\$ 6.67	136,608	\$ 8.90
December 31, 2008	-	\$ -	-	\$ 6.67	67,650	\$ 8.90
Thereafter	-	\$ -	-	\$ 6.67	-	\$ 8.90
Total options exercisable	239,158		15,000		906,900	

We continue to account for stock-based compensation using the intrinsic value method prescribed by APB Opinion No. 25, under which no compensation cost for stock options is recognized for stock option awards granted to employees at or above fair market value. Had compensation expense for the Company's stock compensation plans been determined based upon fair values at the grant dates for awards under the plan in accordance with SFAS No. 123, our net income and net income per share would have been reduced to the pro forma amounts indicated below.

	For the three months ending September 30,		For the nine months ending September 30,	
	2004	2003	2004	2003
Net Income (loss) as reported	\$ (16,946,258)	\$ 1,990,831	\$ (10,347,473)	\$ 6,413,166
Compensation, net of tax effect	6,171,950	865,096	6,714,508	1,125,656
Pro forma net income	\$ (23,118,208)	\$ 1,125,735	\$ (17,061,981)	\$ 5,287,510
Net income per share				
As reported - Basic	\$ (2.86)	\$ 0.42	\$ (1.79)	\$ 1.39
As reported - Diluted	\$ (2.86)	\$ 0.38	\$ (1.79)	\$ 1.32
Pro forma - Basic	\$ (3.90)	\$ 0.24	\$ (2.95)	\$ 1.15
Pro forma - Diluted	\$ (3.90)	\$ 0.21	\$ (2.95)	\$ 1.09

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Additional stock option awards are anticipated in future years.

The weighted average fair value of options granted during the nine months ended September 30, 2004, estimated on the date of grant using the Black-Scholes option-pricing model, was \$18.02. The weighted average fair value of options granted during 2004 and 2003, estimated on the date of grant using the Black-Scholes option-pricing model, was \$6.67 to \$10.74 in 2004 and \$4.21 to \$8.01 in 2003. The fair value of options granted is estimated on the date of grant using the following assumptions:

	<u>September 30, 2004</u>	<u>December 31, 2003</u>
Dividend yield	2.24% to 3.19%	1.96% to 2.10%
Expected volatility	99.65% to 103.20%	105.91% to 108.73%
Risk-free interest rate	2.13% to 3.60%	2.30% to 3.94%
Expected life (in years)	3.00 to 3.60	3.00 to 6.36

Summary information about the Company's stock options outstanding at September 30, 2004:

	<u>Range of Exercise Price</u>	<u>Outstanding at September 30, 2004</u>	<u>Weighted Average Contractual Periods in Years</u>	<u>Weighted Average Exercise Price</u>	<u>Exercisable at September 30, 2004</u>
1998 Plan	\$6.67	239,158	2.29	\$6.67	143,907
2001 Franchise Plan	\$6.67 to \$9.17	15,000	2.86	\$9.17	15,000
2002 Plan	\$8.33 - \$20.00	906,900	3.32	\$10.74	411,126

(9) SUBORDINATED DEBT

On July 31, 2003, we completed a private placement of our 6% Senior Subordinated Notes (the "July 2003 Notes"), which were offered and sold to accredited investors as units consisting of one Note with a principal amount of \$1,000 and warrants (the "Warrant") to purchase shares of our Common Stock. We sold an aggregate of \$7.5 million of 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 pay interest at the annual rate of 6%, are subordinated to senior debt of the Company, and mature on July 31, 2006. Quarterly payments of principal and interest due on the July 2003 Notes may be made in cash or, at our option, in shares of our Common Stock. If paid in shares of Common Stock, the number of shares to be issued shall be determined by dividing the payment due by 95% of the weighted-average volume price for the Common Stock on Nasdaq as reported by Bloomberg Financial Markets ("Bloomberg") for the 20 consecutive trading days preceding the payment date.

We issued Warrants to purchase shares of our Common Stock to the purchasers of the July 2003 Notes and to the placement agent in the offering, J. Giordano Securities Group ("J. Giordano"). Each Warrant entitles the holder to purchase one-half of one share of our Common Stock. The total number of shares issuable upon exercise of Warrants issued to the purchasers of the July, 2003 Notes and to J. Giordano were determined after the expiration of 60 consecutive trading days following July 31, 2003, which was the date of closing of the offering and totaled 408,050. The number of shares issued upon exercise of the Warrants issued to purchasers equaled \$7.5 million divided by the exercise price of the Warrants and totaled 392,356 shares. The number of shares issuable upon exercise of the Warrants issued to J. Giordano equaled \$300,000 divided by the exercise price of the Warrants and totaled 15,694 shares. The exercise price of the Warrants equals 115% of the weighted-average volume price of the Common Stock on Nasdaq as reported by Bloomberg for the 60 consecutive trading days following July 31, 2003, with a maximum of \$25.00 per share and a minimum of \$15.00 per share. As computed, the exercise price of the Warrants equaled \$19.1153. The terms of the Warrants provide for adjustment of the exercise price and the number of shares issuable thereunder upon the occurrence of certain events typical for private offerings of this type. The Warrants will be exercisable until July 31, 2006. GAAP requires that detachable warrants be valued separately from

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debt and included in paid-in capital. Based on the terms of the unit purchase agreement with the investors in the private placement, management believes that the Warrants had zero value at the date of issuance of the July, 2003 Notes.

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 note with a principal amount of \$1,000 and warrants to purchase shares of our common stock, the terms of which are similar to our notes and warrants sold in July 2003, 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 pay interest at the annual rate of 6%, mature on September 30, 2007, and rank pari passu in terms of payment and priority to the 6% Senior Subordinated Notes dated July 31, 2003 in the original principal amount of \$7,500,000 that we sold in 2003. Quarterly payments of principal and interest due on these notes, like the notes we sold in 2003, may be made in cash or, at our option, in shares of our common stock. If paid in shares of common stock, the number of shares to be issued shall be determined by dividing the payment due by 95% of the weighted-average volume price for the common stock on Nasdaq as reported by Bloomberg for the 20 consecutive trading days preceding the payment date.

We also issued warrants to purchase shares of our common stock to the purchasers of the notes and to the placement agent in the offering, J. Giordano Securities Group. Each warrant entitles the holder to purchase one share of our common stock at an exercise price of \$12.75 per share and will be exercisable until September 30, 2007. By comparison, the warrants we sold in 2003 are each exercisable for one-half share of common stock at an exercise price of \$12.74 per whole share. The number of shares issuable upon exercise of the warrants issued to purchasers equaled \$12.5 million divided by the exercise price of the warrants, and totaled 980,392. The number of shares issuable upon exercise of the warrants issued to J. Giordano equaled \$500,000 divided by the exercise price of the warrants, and totaled 39,216. The terms of the warrants provide for adjustment of the exercise price and the number of shares issuable thereunder upon the occurrence of certain events typical for private offerings of this type.

For the July 2003 Notes, quarterly principal and interest payments, totaling approximately \$0.7 million per payment, are due on January 31, April 30, July 31, and October 31 with the last installment due on July 31, 2006. The scheduled loan payments for the July 2003 Notes for the next three years are as follows:

<u>For the period</u>	
Three months ending December 31, 2004	\$ 625,000
Year ending December 31, 2005	2,500,000
Year ending December 31, 2006	<u>1,875,000</u>
Total	<u>\$ 5,000,000</u>

On or about January 31, 2004, April 30, 2004, July 31, 2004 and October 31, 2004, we paid, pursuant to the terms of the July 2003 Notes, the quarterly payments of principal and interest due in shares of our Common Stock and in accordance with the contractual computations issued 54,014; 53,729; 49,965 and 69,200 shares of Common Stock, respectively.

For the September 2004 Notes, quarterly principal and interest payments, totaling approximately \$1.2 million per payment, are due, beginning next year, on January 31, April 30, July 31, and October 31 with the last installment due on September 30, 2007. The scheduled loan payments for the September 2004 Notes for the next three years are as follows:

<u>For the period</u>	
Year ending December 31, 2005	\$ 4,166,668
Year ending December 31, 2006	4,166,668
Year ending December 31, 2007	<u>4,166,664</u>
	<u>\$ 12,500,000</u>

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ITEM 2:

Forward-Looking Statements

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

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

Overview

We are a vertically integrated insurance holding company, which, through our subsidiaries, control substantially all aspects of the insurance underwriting, distribution and claims process. We underwrite personal automobile insurance, general liability insurance, flood insurance, homeowners' insurance and mobile home property and casualty insurance in Florida, Georgia and Louisiana through our wholly owned subsidiaries, Federated National Insurance Company (“Federated National”) and American Vehicle Insurance Company (“American Vehicle”). American Vehicle has recently been authorized to write commercial general liability policies in Kentucky and expects to begin writing policies in that state in the near future. American Vehicle is a fully admitted insurance carrier in Florida and Louisiana and is admitted as a surplus lines carrier in Georgia and Kentucky.

During the nine months ended September 30, 2004, 21.4%, 63.8%, 1.6% and 13.2% of the policies we underwrote were for personal automobile insurance, homeowners' property and casualty insurance, mobile home property and casualty insurance, and commercial general liability, respectively. During the year ended December 31, 2003, 67.5%, 23.0%, 2.4% and 7.1% of the policies we underwrote were for personal automobile insurance, homeowners' property and casualty insurance, mobile home property and casualty insurance, and commercial general liability, respectively. We internally process claims made by our own and third party insureds through our wholly owned claims adjusting company, Superior Adjusting, Inc. (“Superior”). We also offer premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium Finance, Inc. (“Federated Premium”).

We market and distribute our own and third-party insurers' products and our other services primarily in Central and South Florida, through a network of 24 agencies owned by Federated Agency Group, Inc. (“Federated Agency Group”), a wholly owned subsidiary, 45 franchised agencies, approximately 1,500 independent agents and a select number of general agents. Our independent agents and general agents are primarily responsible for the distribution of our homeowner insurance and commercial general liability products. Through our wholly owned subsidiary, FedUSA, Inc. (“FedUSA”), we franchise agencies under the FedUSA name. As of September 30, 2004, franchises were granted to 48 FedUSA agencies, of which 42 were operating and 6 are pending.

Assurance Managing General Agents, Inc. (“Assurance MGA”), a wholly owned subsidiary, acts as Federated National's and American Vehicle's exclusive managing general agent. Assurance MGA currently

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provides all underwriting policy administration, marketing, accounting and financial services to Federated National, American Vehicle and our agencies, and participates in the negotiation of reinsurance contracts. Assurance MGA generates revenue through policy fee income and other administrative fees from the marketing of companies' products through the Company's distribution network. Assurance MGA plans to establish relationships with additional carriers and add additional insurance products in the future.

We offer electronic tax filing services through Express Tax Service, Inc. ("Express Tax"), an 80%-owned subsidiary, as well as franchise opportunities for these services. As of September 30, 2004, there were 252 franchises granted in 19 states. Revenue is generated through franchise sales, collection of royalties on tax preparation fees, incentives from business partners as well as fees from the preparation of income tax returns and income tax refund anticipation loans. In addition, Express Tax offers tax preparation services through approximately 300 licensees nationwide.

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

We operate in a highly competitive market and face competition from both national and regional insurance companies, many of whom are larger and have greater financial and other resources, have better A.M. Best ratings and offer more diversified insurance coverage. Our competitors include other companies which market their products through agents, as well as companies which sell insurance directly to their customers. Large national writers may have certain competitive advantages over agency writers, including increased name recognition, increased loyalty of their customer base and reduced policy acquisition costs. We may also face competition from new or temporary entrants in our niche markets. In some cases, such entrants may, because of inexperience, desire for new business or other reasons, price their insurance below ours. Although our pricing is inevitably influenced to some degree by that of our competitors, we believe that it is generally not in our best interest to compete solely on price. We instead tend to compete on the basis of underwriting criteria, our distribution network and superior service to our agents and insureds. We compete with respect to automobile insurance in Florida with more than 100 companies, which underwrite personal automobile insurance. Comparable companies which compete with us in the personal automobile insurance market include U.S. Security Insurance Company, United Automobile Insurance Company, Direct General Insurance Company and Security National Insurance Company, as well as major insurers such as Progressive Casualty Insurance Company. Comparable companies which compete with us in the homeowners' market include Florida Family Insurance Company, Florida Select Insurance Company, Atlantic Preferred Insurance Company and Vanguard Insurance Company. Comparable companies which compete with us in the general liability insurance market include Century Surety Insurance Company, Atlantic Casualty Insurance Company, Colony Insurance Company and Burlington/First Financial Insurance Companies. Competition could have a material adverse effect on our business, results of operations and financial condition.

Our executive offices are located at 3661 West Oakland Park Boulevard, Suite 300, Lauderdale Lakes, Florida 33313 and our telephone number is (954) 581-9993.

Recent Events

In August and September 2004, the State of Florida experienced four hurricanes, Charley, Frances, Ivan and Jeanne. One of our subsidiaries, Federated National, incurred significant losses relative to its homeowners' insurance line of business. Approximately 7,500 policyholders have filed hurricane-related claims totaling an estimated \$62.0 million, of which we estimate that our share of the costs associated with these hurricanes will be approximately \$33.0 million, net of our reinsurance recoveries.

On June 14, 2004 we announced a 3-for-2 stock split. The stock split was in the form of a stock dividend and was distributed on or about September 7, 2004, to shareholders of record at the close of business on August 23, 2004. Shareholders received three shares of common stock for every two shares of our stock held on the record date. Just prior to the three-for-two stock split, we had approximately 3,957,000 shares outstanding, and following the stock split, we had approximately 5,936,000 shares outstanding, including fractional shares that were paid in common stock. All earnings per share data included in the consolidated financial statements and notes thereto have been restated after giving retroactive effect for the September 7, 2004 three-for-two stock split.

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In August 2004, A.M. Best Company notified us that Federated National and American Vehicle were being placed under review with negative implications. A.M. Best in 2003 had assigned Federated National a B rating ("Fair," which is the seventh of 14 rating categories) and American Vehicle a B+ rating ("Very Good," which is the sixth of 14 rating categories). Federated National and American Vehicle are currently rated "A" ("Unsurpassed," which is first of six ratings) by Demotech, Inc. We will most likely not maintain our A. M. Best ratings due to the recent hurricanes. A downgrade or withdrawal of our ratings could limit or prevent us from writing or renewing desirable insurance policies or from obtaining adequate reinsurance and may limit our expansion plans.

Analysis of Financial Condition
As of September 30, 2004 as Compared to December 31, 2003

Investments

Investments increased \$42.4 million, or 89.6%, to \$89.7 million as of September 30, 2004, as compared to \$47.3 million as of December 31, 2003, primarily as a result of our investment of the proceeds from an increase in written insurance premiums.

As a result of the adverse market conditions that occurred in 2002, management more carefully monitors its concentrations, industries and asset allocations. There were no other instances of large concentrations of investment securities requiring write-downs.

Financial Accounting Standards ("FAS") number 115 addresses accounting and reporting for (a) investments in equity securities that have readily determinable fair values and (b) all investments in debt securities. FAS 115 requires that these securities be classified in three categories and given specific accounting treatment as follows:

<u>Classification</u>	<u>Accounting Treatment</u>
Held-to-maturity Debt securities with the intent and ability to hold to maturity	Amortized cost
Trading securities Debt and equity securities bought and held primarily for sale in the near term	Fair value, with unrealized holding gains and losses included in operations
Available-for-sale Debt and equity securities not classified as held-to-maturity or trading securities	Fair value, with unrealized holding gains and losses excluded from earnings and reported as a separate component of shareholders' equity, namely "Other Comprehensive Income"

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In accordance with the above we have classified all of our investment portfolio as available-for-sale during the nine months ending September 30, 2004 and the year ended December 31, 2003.

Below is a summary of unrealized gains and (losses) at September 30, 2004 and December 31, 2003 by category.

	Unrealized Gains and (Losses)	
	<u>September 30, 2004</u>	<u>December 31, 2003</u>
Fixed maturities:		
U.S. government obligations	\$ (452,464)	\$ (793,613)
Obligations of states and political subdivisions	(6,300)	(4,840)
	<u>(458,764)</u>	<u>(798,453)</u>
Corporate securities:		
Communications	16,632	209,226
Financial	5,300	14,694
Other	79,103	45,475
	<u>101,035</u>	<u>269,395</u>
Equity securities:		
Preferred stocks	(500)	400
Common stocks	(359,249)	3,154
	<u>(359,749)</u>	<u>3,554</u>
Total unrealized gains and (losses)	<u>\$ (717,478)</u>	<u>\$ (525,504)</u>

For further detail, see the section titled ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Receivable for Investments Sold

The receivable for investments sold decreased \$2.0 million, or 94.1%, to \$0.1 million as of September 30, 2004, as compared to \$2.1 million as of December 31, 2003. The decrease is a result of investment trading activity that occurred in late December 2003 and did not settle until early January 2004.

Prepaid Reinsurance Premiums

Prepaid reinsurance premiums decreased \$5.3 million, or 63.4%, to \$3.1 million as of September 30, 2004, as compared to \$8.4 million as of December 31, 2003. The decline reflects a \$7.4 decrease in our insurance subsidiaries' reliance on automobile quota-share reinsurance. During 2003 we ceded 40% of our automobile premiums to our reinsurer, and for the first nine months of 2004, the company has not ceded any automobile premiums. The decrease in prepaid reinsurance premiums was mitigated by an increase of \$2.1 in prepaid catastrophic reinsurance premiums during the same nine-month period ending September 30, 2004.

Reinsurance Recoverable, Net

Reinsurance recoverable, net increased \$23.5 million, or 212.3%, to \$34.5 million as of September 30, 2004, as compared to \$11.0 million as of December 31, 2003. The increase in reinsurance recoverable, net consists of \$28.6 million due to our claims associated with the hurricanes experienced in August and September of 2004 mitigated by a decrease in reinsurance recoverable, net of \$5.1 million.

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Deferred Policy Acquisition Costs

Deferred policy acquisition costs increased \$5.3 million, or 303.2%, to \$7.0 million as of September 30, 2004, as compared to \$1.7 million as of December 31, 2003. For the nine months ended September 30, 2004, commission expense and commission income, net, were approximately \$6.2 million and expenses connected with the writing of premiums such as salaries and premium taxes, net of policy fees, totaled approximately \$0.8 million. Deferred policy acquisition costs increased primarily due to a \$2.7 million increase in deferred commission expenses and a \$2.2 million decrease in ceded unearned commissions income during the nine months ended September 30, 2004. The increase in deferred commission expenses primarily related to the increase in lines of insurance other than automobile, which are not subject to quota-share agreements. The decrease in ceded commissions income is due to a \$7.4 million decline in ceded commissions and is due to the intentional absence of a quota-share agreement in place for premiums written in 2004. Deferred policy acquisition costs was formerly titled Deferred acquisition costs.

Income Taxes Recoverable

Income taxes recoverable increased \$6.4 million, or 775.1%, to \$7.2 million as of September 30, 2004, as compared to \$0.8 million as of December 31, 2003. The increase in Income taxes recoverable consists of the recoupment of estimated 2004 income tax payments paid in 2004 and Federal net operating loss carry-back provisions.

Unpaid Losses and Loss Adjustment Expenses

Unpaid losses and loss adjustment expenses increased \$52.1 million, or 212.0%, to \$76.7 million as of September 30, 2004, as compared to \$24.6 million as of December 31, 2003. The widely publicized hurricanes during August and September of 2004 significantly affected our homeowner line of insurance products. Approximately 7,500 policyholders have filed hurricane related claims totaling an estimated \$62.0 million of which we estimate that our share of the costs associated with these hurricanes will be approximately \$33.0 million. Our Automobile and Commercial General Liability insurance products were not materially affected by the hurricanes. As of September 30, 2004, approximately \$9.1 million has been received by us to settle hurricane losses and is reflected on our consolidated balance sheet at September 30, 2004 as Funds held under reinsurance treaties. The remainder of our expected incurred losses associated with the four hurricanes is recorded as part of our Unpaid Losses and Loss Adjustment Expenses. The following schedule reflects the activity in the liability for unpaid losses and loss adjustment expenses for the nine months ending September 30, 2004 and December 31, 2003.

	<u>September 30, 2004</u>	<u>December 31, 2003</u>
Balance at January 1:	\$ 24,570,198	\$ 16,983,756
Less reinsurance recoverables	<u>(9,761,354)</u>	<u>(7,847,421)</u>
Net balance at January 1	<u>\$ 14,808,844</u>	<u>\$ 9,136,335</u>
 Incurred related to:		
Current year	\$ 57,845,208	\$ 26,274,932
Prior years	<u>(103,995)</u>	<u>1,234,047</u>
Total incurred	<u>\$ 57,741,213</u>	<u>\$ 27,508,979</u>
 Paid related to:		
Current year	\$ 17,796,300	\$ 14,205,212
Prior years	<u>9,145,184</u>	<u>7,631,258</u>
Total paid	<u>\$ 26,941,484</u>	<u>\$ 21,836,470</u>
 Net balance at year-end	\$ 45,608,573	\$ 14,808,844
Plus reinsurance recoverables	<u>31,045,047</u>	<u>9,761,354</u>
Balance at year-end	<u>\$ 76,653,620</u>	<u>\$ 24,570,198</u>

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

Unearned Premiums

Unearned premiums increased by \$14.4 million or, 42.0%, to \$48.5 million as of September 30, 2004, as compared to \$34.1 million as of December 31, 2003. The increase was due to a \$20.4 million increase in unearned homeowner's insurance premiums and \$2.6 million in unearned premiums associated with the commercial liability program. Offsetting these increases was a \$8.7 million decrease in automobile unearned premiums. These changes reflect our emphasis on property and commercial general liability insurance products. During the quarter ending June 30, 2004, our plans to assume homeowner policies from the insurer created by the State of Florida, Citizens Property Insurance Corporation ("Citizens"), came to fruition. Of the \$20.4 million increase in our homeowner's insurance unearned premiums as of September 30, 2004, 30.5 %, or \$6.2 million relates to our assumption of homeowner insurance policies from Citizens.

Funds Held Under Reinsurance Treaties

Funds held under reinsurance treaties increased by \$9.1 million, or 100% as of September 30, 2004. The increase reflects funds advanced to us under our reinsurance treaties by our reinsurers to pay hurricane related claims. Our obligation, pursuant to the reinsurance contracts, is to pay the first \$10.0 million for each event before we are permitted to use the funds held under our reinsurance treaties.

Results of Operations

Three Months Ended September 30, 2004 as Compared to Three Months Ended September 30, 2003

Gross Premiums Written

Gross premiums written increased \$1.9 million, or 8.6%, to \$24.3 million for the three months ended September 30, 2004, as compared to \$22.4 million for the comparable period in 2003. The following table denotes gross premiums written by major product line.

	<u>Three months ended September 30,</u>			
	<u>2004</u>		<u>2003</u>	
Automobile	\$ 4,045,750	16.6%	\$ 13,960,744	62.4%
Homeowners'	16,564,249	68.2%	5,356,294	23.9%
Commercial liability	3,389,016	13.9%	2,664,980	11.9%
Mobile home owners'	<u>302,785</u>	<u>1.3%</u>	<u>387,211</u>	<u>1.8%</u>
Gross written premiums	<u>\$ 24,301,800</u>	<u>100.0%</u>	<u>\$ 22,369,229</u>	<u>100.0%</u>

As noted above, our efforts to expand our lines of insurance products to emphasize products other than automobile insurance are coming to fruition. Furthermore, our assumption of policies from Citizens during the three months ended September 30, 2004 totaled 10.4% or \$2.5 million of the \$24.3 million of gross written premiums.

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Gross Premiums Ceded

Gross premiums ceded decreased \$5.7 million to \$0.1 million for the three months ended September 30, 2004, as compared to a charge to operations of \$5.6 million for the three months ended September 30, 2003. The decrease is due to the decline in our ceded quota-share reinsurance associated with our automobile insurance. For the quarter ended September 30, 2004, we did not cede any automobile insurance premiums, as compared to a 40% cession for the same period last year.

Increase (Decrease) in Prepaid Reinsurance Premiums

The change in the increase (decrease) in prepaid reinsurance premiums was \$3.2 million, or \$0.8 million for the three months ended September 30, 2004, compared to (\$2.5) million for the three months ended September 30, 2003. The increase is due to the intentional absence of a quota-share agreement in place for premiums written in 2004 totaling \$1.2 million and an increase in our catastrophic insurance premiums totaling \$2.1 million.

Decrease (Increase) in Unearned Premiums

Unearned premiums decreased by \$2.6 million to (\$0.2) million as of September 30, 2004, as compared to a charge to operations of \$2.4 million as of September 30, 2003. The decrease was due to a \$2.4 million increase in unearned homeowners' insurance premiums and \$0.6 million in unearned premiums associated with the commercial liability insurance program. Offsetting these increases was a \$3.0 million decrease in automobile unearned premiums.

Net Investment Income

Net investment income increased by \$0.3 million, or 63.5%, to \$0.8 million for the three months ended September 30, 2004, as compared to \$0.5 million for the same three month period ended September 30, 2003. The increase in investment income is a result of the additional amounts of invested assets. Also affecting our net investment income were our declining yields of 3.99% for the three months ended September 30, 2004 as compared to 4.83% for the three months ended September 30, 2003.

Net Realized Investment Gains

Net realized investment gains increased by \$.05 million, or 139.8% to \$0.08 million for the three months ended September 30, 2004, as compared to \$.03 million for the three months ended September 30, 2003. The table below depicts the gains by investment category.

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	Net Realized Gains (Losses)	
	<u>Three Months Ended September 30,</u>	
	<u>2004</u>	<u>2003</u>
Fixed maturities:		
U.S. government obligations	\$ (32,116)	\$ (209,334)
Obligations of states and political subdivisions	(10,450)	-
	<u>(42,566)</u>	<u>(209,334)</u>
Corporate securities:		
Communications	-	79,248
Financial	-	(693)
Other	-	(78,557)
	<u>-</u>	<u>(2)</u>
Equity securities:		
Preferred stocks	(56)	-
Common stocks	123,581	243,101
	<u>123,525</u>	<u>243,101</u>
Total net realized gains (losses)	<u>\$ 80,959</u>	<u>\$ 33,765</u>

Loss and Loss Adjustment Expenses

Loss and loss adjustment expenses increased by \$36.0 million, or 568.9%, to \$42.3 million for the three months ended September 30, 2004, as compared to \$6.3 million as of September 30, 2003. The widely publicized hurricane season significantly affected our homeowner line of insurance products. Approximately 7,500 policyholders have filed hurricane related claims totaling an estimated \$62.0 million of which we estimate that our share of the costs associated with these hurricanes will be approximately \$33.0 million. Our Automobile and Commercial General Liability insurance products were not materially affected by the hurricanes. Our loss ratio, as determined in accordance with GAAP, for the three-month period ended September 30, 2004 was 167.22% compared with 53.35% for the same period in 2003. The table below reflects the loss ratios by product line.

	<u>Three months ending September 30,</u>	
	<u>2004</u>	<u>2003</u>
Automobile	114.52%	65.88%
Home owners	196.22%	25.36%
Commercial liability	9.86%	50.32%
Mobile home owners	777.05%	24.44%
All product lines	167.22%	53.35%

Losses and loss adjustment expense, 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. Management revises its estimates based on the results of its 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.

Operating and Underwriting Expenses

Operating and underwriting expenses rose by \$4.5 million, or 150.6%, to \$7.4 million for the three months ended September 30, 2004, as compared to \$3.0 million for the three months ended September 30, 2003. The increase is primarily associated with our cost of obtaining various types of insurance products, as well as an assessment pursuant to our participation in an insurance apportionment plan.

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Policy Acquisition Costs, Net of Amortization

Policy acquisition costs, net of amortization, increased by \$2.4 million, charging earnings \$2.5 million for the three months ended September 30, 2004, as compared to a charge to earnings of \$0.12 million as of September 30, 2003. 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 attributable to premiums earned during the period.

During the three months ended September 30, 2004, the difference between the ceded commissions earned of \$0.4 million and amortized costs of \$2.9 million resulted in a charge to earnings of \$2.5 million. The \$2.4 million increase in the amortization of deferred policy acquisition costs in the 2004 period as compared to the 2003 period is attributable to the decrease in ceded commissions earned totaling \$1.1 million, and increased amortized costs of \$1.3 million during the three month period ended September 30, 2004. Policy acquisition costs, net of amortization was formerly titled Amortization of deferred acquisition costs, net.

Provision (Benefit) for Income Tax Expense

There was an income tax benefit for the three months ended September 30, 2004, compared with a provision for income taxes for the same three-month period last year. The income tax benefit is a result of the losses incurred during the third quarter of 2004. The benefit reflects our ability to carry-back our Federal income taxes and carry-forward our Florida income taxes.

Results of Operations

Nine Months Ended September 30, 2004 as Compared to Nine Months Ended September 30, 2003

Gross Premiums Written

Gross premiums written increased \$17.4 million, or 30.7%, to \$73.9 million for the nine months ended September 30, 2004, as compared to \$56.6 million for the comparable period in 2003. The following table denotes gross premiums written by major product line.

	<u>Nine months ended September 30,</u>			
	<u>2004</u>		<u>2003</u>	
Automobile	\$ 15,824,076	21.4%	\$ 39,915,374	70.6%
Homeowners'	47,131,793	63.8%	12,614,755	22.3%
Commercial liability	9,762,931	13.2%	2,664,980	4.7%
Mobile home owners'	<u>1,210,771</u>	<u>1.6%</u>	<u>1,364,694</u>	<u>2.4%</u>
Gross written premiums	<u>\$ 73,929,571</u>	<u>100.0%</u>	<u>\$ 56,559,803</u>	<u>100.0%</u>

As noted above, our efforts to expand our lines of insurance products to emphasize products other than automobile insurance are coming to fruition. Furthermore, our assumption of policies from Citizens during the nine months ended September 30, 2004 totaled 18.4% or \$13.6 million of the \$73.9 million of gross written premiums as of September 30, 2004.

Gross Premiums Ceded

Gross premiums ceded decreased \$16.8 million to \$1.0 million for the nine months ended September 30, 2004, as compared to a charge to operations of \$15.8 million for the nine months ended September 30, 2003. The decrease is due to the decline in our ceded quota-share reinsurance associated with our automobile insurance. For the quarter ended September 30, 2004, we did not cede any automobile insurance premiums, as compared to a 40% cession for the same period last year.

Increase (Decrease) in Prepaid Reinsurance Premiums

The change in the increase (decrease) in prepaid reinsurance premiums was a decrease of \$2.8 million, or (\$5.3) million for the nine months ended September 30, 2004, compared to (\$2.5) million for the nine months ended

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September 30, 2003. The increase is due to the intentional absence of a quota-share agreement in place for premiums written in 2004 totaling \$1.2 million and an increase in our catastrophic insurance premiums totaling \$2.1 million.

Decrease (Increase) in Unearned Premiums

Unearned premiums increased by \$9.4 million to (\$14.3) million as of September 30, 2004, as compared to (\$4.9) million as of September 30, 2003. The increase was due to a \$15.5 million increase in unearned homeowners' insurance premiums and \$0.3 million in unearned premiums associated with the commercial liability insurance program. Offsetting these increases was a \$6.3 million decrease in automobile unearned premiums.

Net Investment Income

Net investment income increased by \$0.9 million, or 74.2%, to \$2.1 million for the nine months ended September 30, 2004, as compared to \$1.2 million for the same nine month period ended September 30, 2003. The increase in investment income is a result of the additional amounts of invested assets. Also affecting our net investment income are the declining yields of 0.51% for the nine months ended September 30, 2004 as compared to 5.23% for the nine months ended September 30, 2003.

Net Realized Investment Gains

Net realized investment gains decreased by \$1.2 million, or 82.0% to \$0.3 million for the nine months ended September 30, 2004, as compared to \$1.5 million for the nine months ended September 30, 2003. The table below depicts the gains by investment category.

	Net Realized Gains	
	<u>Nine Months Ended September 30,</u>	
	<u>2004</u>	<u>2003</u>
Fixed maturities:		
U.S. government obligations	\$ 30,397	\$ 291,427
Obligations of states and political subdivisions	<u>(10,566)</u>	<u>345,177</u>
	<u>19,831</u>	<u>636,604</u>
Corporate securities:		
Communications	-	118,107
Financial	(219)	88,683
Other	<u>-</u>	<u>57,453</u>
	<u>(219)</u>	<u>264,243</u>
Equity securities:		
Preferred stocks	(56)	23,555
Common stocks	<u>241,830</u>	<u>529,063</u>
	<u>241,774</u>	<u>552,618</u>
Total net realized gains	<u>\$ 261,386</u>	<u>\$ 1,453,465</u>

Loss and Loss Adjustment Expenses

Loss and loss adjustment expenses increased by \$35.7 million, or 173.7%, to \$56.4 million for the nine months ended September 30, 2004, as compared to \$20.6 million as of September 30, 2003. The widely publicized hurricane season significantly affected our homeowners' line of insurance products. Approximately 7,500 policyholders have filed hurricane-related claims totaling an estimated \$62.0 million, of which we estimate that our share of the costs associated with these hurricanes will be approximately \$33.0 million. Our automobile and commercial general liability insurance products were not materially affected by the hurricanes. Our loss ratio, as determined in accordance with GAAP, for the nine month period ended September 30, 2004 was 106.11% compared

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with 61.95% for the same period in 2003. The table below reflects the loss ratios by product line.

Losses and loss adjustment expense, our most significant expense, represents 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. Management revises its estimates based on the results of its 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. We attribute the "all lines" decrease in the loss ratio primarily to the increasingly significant operational contributions made by our lines of insurance other than automobile.

	<u>Nine months ending September 30,</u>	
	<u>2004</u>	<u>2003</u>
Automobile	90.87%	77.84%
Home owners	121.89%	18.94%
Commercial liability	17.70%	24.44%
Mobile home owners	281.41%	35.06%
All product lines	106.11%	61.95%

Operating and Underwriting Expenses

Operating and underwriting expenses rose by \$5.6 million, or 67.3%, to \$13.9 million for the nine months ended September 30, 2004, as compared to \$8.3 million for the nine months ended September 30, 2003. The increase is primarily associated with our cost of obtaining various types of insurance products, as well as an assessment pursuant to our participation in a insurance apportionment plan.

Policy Acquisition Costs, Net of Amortization

Policy acquisition costs, net of amortization, increased by \$5.6 million, charging earnings by \$4.6 million for the nine months ended September 30, 2004, as compared to a credit of \$0.9 million as of September 30, 2003. 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 attributable to premiums earned during the period.

During the nine months ended September 30, 2004, the difference between the ceded commissions earned of \$1.9 million and amortized costs of \$6.5 million resulted in a charge to earnings of \$4.6 million. The \$3.7 million increase in the amortization of deferred policy acquisition costs in the 2004 period as compared to the 2003 period is attributable to the decrease in ceded commissions earned totaling \$7.2 million, and increased amortized costs of \$10.9 million during the nine month period ended September 30, 2004. Policy acquisition costs, net of amortization was formerly titled Amortization of deferred acquisition costs, net.

Provision (Benefit) for Income Tax Expense

There was an income tax benefit for the nine months ended September 30, 2004, compared with a provision for income taxes for the same nine-month period last year. The income tax benefit is a result of the losses incurred during the third quarter of 2004. The benefit reflects our ability to carry-back our Federal income taxes and carry-forward our Florida income taxes.

Liquidity and Capital Resources

Our primary sources of capital during the nine months ended September 30, 2004 are revenues generated from operations, issuance of debt securities, investment income and borrowings under the Revolving Agreement, described below. Because we are a holding company, we are largely dependent upon fees from our subsidiaries for cash flow.

Federated Premium's operations are funded by a revolving loan agreement ("Revolving Agreement") with FlatIron Funding Company LLC ("FlatIron"). The Revolving Agreement is structured as a sale of contracts receivable under a sale and assignment agreement with FPF, Inc., a wholly-owned subsidiary of FlatIron ("FPF"), which gives FPF the right to sell or assign these contracts receivable. Federated Premium, which services these

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contracts, has recorded transactions under the Revolving Agreement as secured borrowings.

During September 2004, we negotiated a new revolving loan agreement in which the maximum credit commitment available to us was reduced at our request to \$2.0 million with built-in options to incrementally increase the maximum credit commitment up \$4.0 million over the next three years. We believe that this available credit is sufficient based on our current operations. Our lender, however, could decide to reduce our available credit based on a number of factors, including the A.M. Best ratings of Federated National and American Vehicle. If the A.M. Best rating of Federated National falls below a "C," or if the financial condition of American Vehicle, as determined by our lender in its sole discretion suffers a material adverse change, then under the terms of the Revolving Agreement, policies written by that subsidiary will no longer be eligible collateral, causing our available credit to be reduced. If that occurs and we are not able to obtain working capital from other sources, then we would have to restrict our growth and, possibly, our operations.

The amount of FPF's advances are subject to availability under a borrowing base calculation, with maximum advances outstanding not to exceed the maximum credit commitment. The annual interest rate on advances under the Revolving Agreement is the prime rate plus additional interest varying from 1.25% to 3.25% based on the prior month's ratio of contracts receivable related to insurance companies with an A. M. Best rating of B or lower to total contracts receivable. As of September 30, 2004, our interest rate was 4.75% as compared to our interest rate as of September 30, 2003 of 5.75%.

The Revolving Agreement contains various operating and financial covenants, with which we were in compliance at September 30, 2004 and December 31, 2003. Outstanding borrowings under the Revolving Agreement as of September 30, 2004 and December 31, 2003 were \$1.3 million and \$4.1 million, respectively. Outstanding borrowings in excess of the \$4.0 million commitment totaled \$98,786 as of December 31, 2003. The excess amount, permissible by reason of a compensating cash balance of \$200,430 for December 31, 2003, was held for the benefit of FPF and is included in other assets. Interest expense on the Revolving Agreement for the nine months ended September 30, 2004 and 2003 totaled approximately \$150,000 and \$156,000, respectively. For the nine months ended September 30, 2004 and 2003 the effective interest rate on this line of credit, based on our average outstanding borrowings under the Revolving Agreement, was 6.97% and 5.90%, respectively.

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

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

The 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 entitle the holder to purchase $\frac{3}{4}$ of one share of our Common Stock at an exercise price of \$12.7435 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 408,050. GAAP requires that detachable warrants be valued separately from debt and included in paid-in capital. Based on the terms of the purchase agreement with the investors in the private placement, management believes that the 2003 Warrants had zero value at the date of issuance.

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

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

The 2004 Warrants issued to the purchasers of the September 2004 Notes and to the placement agent in the offering, J. Giordano, each entitle the holder to purchase one share of our Common Stock at an exercise price of \$12.75 per share and will be exercisable until September 30, 2007. The number of shares issuable upon exercise of the 2004 Warrants issued to purchasers equaled \$12.5 million divided by the exercise price of the warrants, and totaled 980,392. The number of shares issuable upon exercise of the 2004 Warrants issued to J. Giordano equaled \$500,000 divided by the exercise price of the warrants, and totaled 39,216. The terms of the 2004 Warrants provide for adjustment of the exercise price and the number of shares issuable thereunder upon the occurrence of certain events typical for private offerings of this type.

On or about October 31, 2003, January 31, 2004, April 30, 2004, July 31, 2004 and October 31, 2004, we paid, pursuant to the terms of the July 2003 Notes, the quarterly payments of principal and interest due in shares of our Common Stock and in accordance with the contractual computations issued 61,792, 54,014, 53,729, 49,965 and 69,200 shares of Common Stock, respectively.

For the September 2004 Notes, quarterly principal and interest payments, totaling approximately \$1.2 million per payment, are due beginning next year on January 31, April 30, July 31, and October 31, with the last installment due on September 30, 2007.

For the nine months ended September 30, 2004, operations generated net operating cash flow of \$40.8 million as compared to \$12.9 million for the nine months ended September 30, 2003. Gross cash flow provided by operations generated approximately \$87.2 million, mostly by an increase of unpaid losses and loss adjustment expenses totaling \$52.1 million. Other cash was provided by a \$14.3 million increase in unearned premiums and \$9.1 million received and reflected as funds held under reinsurance treaties. Additional cash was provided by operating activities from prepaid reinsurance premiums totaling \$5.3 million and premium deposits totaling \$1.9 million, in conjunction with premiums receivable of \$1.6 million and financed contracts receivable of \$1.3 million. Uses of cash during the nine months ended September 30, 2004 included \$23.5 million due from reinsurance, net; \$7.2 million due from income taxes deferred and recoverable; \$5.3 million for policy acquisition costs, net of amortization; in conjunction with net losses of \$10.3 million. For the nine months ended September 30, 2003, operations generated net operating cash flow of \$15.0 million as compared to \$12.0 million for the same nine months ending September 30, 2003. Gross cash flow from operations generated approximately \$25.2 million, mostly by an increase in unpaid loss and loss adjustment expenses totaling \$7.0 million, increased unearned premiums liability totaling \$4.9 million, increased prepaid reinsurance premiums totaling \$2.6 million and exercised stock options totaling \$2.3 million, in conjunction with net income of \$6.4 million. We do not expect our operations to generate positive cash flow in the fourth quarter as the Company settles its claims relating the four hurricanes that occurred in August and September of 2004. We currently expect positive operating cash flow to resume during 2005.

Our investment portfolio is highly liquid as it consists almost entirely of readily marketable securities. Cash flow used in net investing activities was \$41.2 million and \$20.9 million for the nine months ended September 30, 2004 and September 30, 2003, respectively. We anticipate that cash flow will be provided by investing activities during the fourth quarter of 2004, because the Company expects to liquidate certain of its investments to settle claims relating the four hurricanes that occurred in August and September 2004. We currently expect cash flow used in investing activities to resume during 2005.

Net cash provided by financing activities was \$11.0 million for the nine months ended September 30, 2004, primarily reflecting the sale of the September 2004 Notes. Other cash sources include \$2.7 million from the exercise of stock options. Cash used in financing activities include \$2.8 million for revolving credit outstanding and \$1.4 million used to pay dividends. Net cash generated from financing activities was \$4.8 million for the nine

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months ended September 30, 2003. This primarily reflected the receipt of \$6.9 million from the issuance of the July 2003 Notes, offset by \$0.8 million paid in dividends and \$1.5 million paid to reduce the revolving credit outstanding. The Company believes that its current capital resources, including the net proceeds from the sale of its July 2003 and September 2004 Notes described above, together with cash flow from the Company's operations, will be sufficient to meet its currently anticipated working capital requirements. There can be no assurances, however, that such will be the case.

To retain our certificates of authority, Florida insurance laws and regulations require that Federated National and American Vehicle maintain capital surplus equal to the greater of 10% of its liabilities or the 2003 statutory minimum capital and surplus requirement of \$3.60 million as defined in the Florida Insurance Code. As of September 30, 2004, Federated National was not in compliance with its requirement to maintain capital surplus equal to the greater of 10% of its liabilities by approximately \$0.3 million. Based on Federated National's payment patterns associated with the settlement of its claims, compliance with the 10% provision has been fully restored by the filing of this Report and the Company does not currently anticipate any regulatory action relative to this matter. American Vehicle remains in compliance with statutory minimum capital and surplus requirement.

The insurance companies are also required to adhere to prescribed premium-to-capital surplus ratios. As of September 30, 2004, Federated National did not comply with the prescribed premium-to-capital surplus ratio, primarily based on the incurred losses associated with the four hurricanes that occurred in August and September 2004. Pursuant to verbal representations made to us by senior officials from the Florida Office of Insurance Regulation ("OIR") of the Florida Department of Financial Services, strict adherence to the prescribed premium-to-capital surplus ratio requirement may not be immediately imposed. The Company is in regular communications with the OIR and has complied with their verbal requests and has relied on their verbal representation that immediate regulatory action will not be imposed relative to its non-compliance with the prescribed premium-to-capital surplus ratio. American Vehicle is in compliance with the prescribed premium-to-capital surplus ratios.

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 Department of Financial Services 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 Department of Financial Services (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 Department of Financial Services 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 Department of Financial Services or (ii) 30 days after the Florida Department of Financial Services 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 during the nine months ending September 30, 2004 or the year ending December 31, 2003, and none are anticipated to be paid in 2005. 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 Department of Financial Services will allow any dividends in excess of the amount available to be paid by Federated National or American Vehicle 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. The ability to pay dividends 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

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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.

Insurance companies are required to comply with the risk-based capital requirements of the National Association of Insurance Commissioners ("NAIC"). The NAIC's risk-based capital requirements are a method of measuring the amount of capital appropriate for an insurance company to support its overall business operations in light of its size and risk profile. NAIC's risk-based capital standards are used by regulators to determine appropriate regulatory actions relating to insurers who show signs of weak or deteriorating condition. Based on calculations using the appropriate NAIC formula and the respective insurance company data for the year ended December 31, 2003, both of the insurance companies total adjusted capital were in excess of ratios that would require regulatory action. GAAP differs in some respects from statutory reporting practices prescribed or permitted by the Florida Department of Financial Services. Federated National's and American Vehicle's statutory capital surplus levels as of September 30, 2004 were approximately \$8.0 million and \$15.0 million, respectively, and their statutory net income (loss) for the nine months ended September 30, 2004 was (\$16.6) million and \$0.2 million, respectively.

Federated National entered into an agreement with the insurer created by the State of Florida, Citizens, to assume the unexpired portion of specifically chosen homeowner insurance policies on varying dates during May, June and July 2004. As part of the assumption agreement, certain provisions provide for a "take out" bonus to be paid to Federated National based upon the successful retention of the assumed policies for the next three years, subject to certain qualifications. Citizens has agreed to fund an escrow account in the name of both Citizens and Federated National in accordance with the contract provisions; however, Federated National is prevented from recognizing the take-out bonus until it has fulfilled its policyholder retention responsibilities, which is expected to be some time subsequent to May 2007. As of September 30, 2004, the escrow account has been funded for \$2.9 million and, in accordance with GAAP, is not included in either our consolidated balance sheet or our consolidated statements of operations.

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. The primary assets and liabilities of the Company are monetary in nature. As a result, interest rates have a more significant impact on our 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 loss adjustment expenses.

Insurance premiums are established before we know the amount of loss and loss adjustment expense 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 increased levels of inflation could cause increases in the dollar amount of incurred loss and loss adjustment expenses and thereby materially adversely affect future liability requirements.

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Item 3. Quantitative and Qualitative Disclosures About Market Risk

Information related to quantitative and qualitative disclosures about market risk was included under Item 7a, "Quantitative and Qualitative Disclosures about Market Risk," in our Annual Report on Form 10-K as of December 31, 2003. No material changes have occurred in market risk since this information was disclosed except as discussed below.

Our investment portfolio is available for sale and is carried at fair value. Gains that represent securities with a fair value in excess of amortized cost, and losses (amortized cost is in excess of fair value) that are deemed temporary by management, are recorded in shareholders' equity in accumulated other comprehensive income. Losses that are deemed other than temporary by management are recorded as net realized losses in the consolidated statement of operations. A summary of the investment portfolio as of September 30, 2004 follows:

	<u>Amortized Cost</u>		<u>Fair Value</u>		<u>Unrealized Gain (Loss)</u>
Fixed maturities:					
U.S. government obligations	\$ 54,729,524	60.55%	\$ 54,277,060	60.52%	\$ (452,464)
Obligations of states and political subdivisions	<u>21,623,036</u>	<u>23.92%</u>	<u>21,616,736</u>	<u>24.11%</u>	<u>(6,300)</u>
	<u>76,352,560</u>	<u>84.47%</u>	<u>75,893,796</u>	<u>84.63%</u>	<u>(458,764)</u>
Corporate securities:					
Communications	1,190,007	1.31%	1,197,663	1.34%	7,656
Financial	1,800,000	1.99%	1,805,300	2.01%	5,300
Other	<u>3,711,787</u>	<u>4.11%</u>	<u>3,799,866</u>	<u>4.24%</u>	<u>88,079</u>
	<u>6,701,794</u>	<u>7.41%</u>	<u>6,802,829</u>	<u>7.59%</u>	<u>101,035</u>
Equity securities:					
Preferred stocks	50,000	0.06%	49,500	0.05%	(500)
Common stocks	<u>7,290,153</u>	<u>8.06%</u>	<u>6,930,904</u>	<u>7.73%</u>	<u>(359,249)</u>
	<u>7,340,153</u>	<u>8.12%</u>	<u>6,980,404</u>	<u>7.78%</u>	<u>(359,749)</u>
Total fixed, corporate and equity securities	<u>\$ 90,394,507</u>	<u>100.00%</u>	<u>\$ 89,677,029</u>	<u>100.00%</u>	<u>\$ (717,478)</u>

As of September 30, 2004, there was one obligation of a state subdivision that represented approximately 7% of the amortized cost of the entire investment portfolio.

Item 4. Controls And Procedures

Evaluation of Disclosure Controls and Procedures

An evaluation of the effectiveness of the design and operation of our disclosure controls and procedures within 90 days of this report was carried out by us under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures have been designed and are being operated in a manner that provides reasonable assurance that the information required to be disclosed by us in reports filed 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. Nevertheless, the controls system, no matter how well designed and operated, cannot provide absolute assurance that the objectives of the controls system are met, and no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected.

Changes in Internal Controls

Subsequent to the date of the most recent evaluation of our internal controls, there were no significant changes in our internal controls or in other factors that could significantly affect the internal controls, including any corrective actions with regard to significant deficiencies and material weaknesses.

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Other Information

PART II: OTHER INFORMATION

Item 1.

Legal Proceedings

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

In June 2000, a lawsuit was filed against us, our directors and our executive officers seeking compensatory damages in an undisclosed amount on the basis of allegations that our amended registration statement dated November 4, 1998 was inaccurate and misleading concerning the manner in which we recognized ceded insurance commission income, in violation of Sections 11 and 15 of the Securities Act of 1933 and Sections 10(b) and 20(a) of the Securities Exchange Act of 1934. The lawsuit was filed in the United States District Court for the Southern District of New York. The plaintiff class purportedly includes purchasers of our common stock between November 5, 1998 and August 13, 1999. The Court granted the plaintiffs class status.

Specifically, the plaintiffs allege that we recognized ceded commission income on a written basis, rather than amortized on a pro rata basis. The plaintiffs allege that this was contrary to the Statement of Financial Accounting Concepts Nos. 1, 2 and 5. We believe, however, that the lawsuit is without merit and we have vigorously defended the action, because we reasonably relied upon outside subject matter experts to make these determinations at the time. We have also since accounted for ceded commissions on a pro rata basis and have done so since these matters were brought to our attention in 1998. Nevertheless, we have also continued to actively participate in settlement negotiations with the plaintiffs and have tentatively agreed to settle the case. The parties are currently negotiating the final terms of a Memorandum of Understanding, which will have to be executed by the parties and then approved by the court. We have reserved and charged against fourth quarter 2003 earnings \$600,000 for the potential settlement and associated costs.

Item 2.

Unregistered Sales of Equity Securities and Use of Proceeds

On July 31, 2004 and October 31, 2004 we issued an aggregate of 49,965 and 69,200 shares, respectively, of our common stock to holders of our Notes in payment of the quarterly interest and principal payments due pursuant to the terms of the Notes. These shares were issued without registration under the Securities Act of 1933 (the "Act") by reason of the exemption from registration pursuant to Section 4(2) of the Act and Regulation D thereunder.

On September 30, 2004, we completed a private placement of our September 2004 Notes and 2004 Warrants (see "Liquidity and Capital Resources" under Item 2, Management's Discussion and Analysis of Financial Condition and Results of Operations, above). These securities were issued without registration under the Act by reason of the exemption from registration pursuant to Section 4(2) of the Act and Regulation D thereunder.

Item 3.

Defaults Upon Senior Securities

None.

Item 4.

Submission of Matters to a Vote of Security Holders

None.

Item 5

Other Information

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Other Information

None.

Item 6

Exhibits

- 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.

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Other Information**

Signatures

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

21st CENTURY HOLDING COMPANY

By: /s/ Richard A. Widdicombe
Richard A. Widdicombe, Chief Executive Officer

/s/ James G. Jennings III
James G. Jennings III, Treasurer and Chief Financial Officer

Date: November 15, 2004

21st Century Holding Company

EXHIBIT 31.1

CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 302 OF THE SARBANES- OXLEY ACT

I, Richard A. Widdicombe, certify that:

1. I have reviewed this quarterly report on Form 10-Q of 21st Century Holding Company;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosures controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluations; and
 - c) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that was materially affected, or is reasonably likely to materially affect, the registrant's control over financial reporting; and;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 15, 2004.

/s/ Richard A. Widdicombe
Chief Executive Officer

21st Century Holding Company

EXHIBIT 31.2

CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT

I, James G. Jennings III, certify that:

1. I have reviewed this quarterly report on Form 10-Q of 21st Century Holding Company;
2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;
3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and we have:
 - a) designed such disclosure controls and procedures, or caused such disclosures controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this quarterly report based on such evaluations; and
 - c) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter that was materially affected, or is reasonably likely to materially affect, the registrant's control over financial reporting; and;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
 - a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 15, 2004.

/s/ James G. Jennings, III
Treasurer and Chief Financial Officer

21st Century Holding Company

EXHIBIT 32.1

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER PURSUANT TO SECTION 906 OF
THE SARBANES-OXLEY ACT**

In connection with the Quarterly Report on Form 10-Q of 21st Century Holding Company for the quarter ended September 30, 2004 as filed with the Securities and Exchange Commission (the "Report"), I, Richard A. Widdicombe, Chief Executive Officer of 21st Century Holding Company, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of 21st Century Holding Company.

By: /s/ Richard A. Widdicombe
Richard A. Widdicombe, Chief Executive Officer

21st Century Holding Company

EXHIBIT 32.2

**CERTIFICATION OF CHIEF FINANCIAL OFFICER PURSUANT TO SECTION 906 OF
THE SARBANES-OXLEY ACT**

In connection with the Quarterly Report on Form 10-Q of 21st Century Holding Company for the quarter ended September 30, 2004 as filed with the Securities and Exchange Commission (the "Report"), I, James G. Jennings, III, Treasurer and Chief Financial Officer of 21st Century Holding Company, hereby certify pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of 21st Century Holding Company.

By: /s/ James G. Jennings, III

James G. Jennings, III, Treasurer and Chief Financial Officer