21ST CENTURY HOLDING CO
Form 10-K
March 30, 2012

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

FORM 10-K

ý Annual Report under Section 13 or 15(d) of the Securities Act of 1934
For the fiscal year ended December 31, 2011

or

o Transition Report under Section 13 or 15(d) of the Securities Exchange Act of 1934
For the transition period of _____________to_______________
Commission file number: 0-2500111

21st Century Holding Company
(Exact name of registrant as specified in its Charter)

Florida	65-0248866
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No)

14050 N.W. 14th Street, Suite 180, Sunrise, Florida 33323
(Address of principal executive offices) (Zip Code)

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

Securities registered pursuant to Section 12(b) of the Exchange Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, par value $0.01 per share	NASDAQ Global Market, LLC

Securities registered pursuant to Section 12(g) of the Exchange Act:
None

Indicate by check mark if the Registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No ý

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yesý No o

Indicate by check mark whether the registrant has electronically submitted and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Sec.232.405 of this chapter) during the preceding 12 months (or for such shorter period that the Registrant was required to submit and post such files). Yes ý No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definition of “large accelerated filer,” “accelerated filer,” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer o	Accelerated filer o	Non-accelerated filer o	Smaller reporting company ý

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Act). Yeso No ý

The aggregate market value of the Registrant’s common stock held by non-affiliates was $20,202,003 on June 30, 2011, computed on the basis of the closing sale price of the Registrant’s common stock on that date.

As of March 30, 2012, the total number of common shares outstanding of Registrant's common stock was 7,946,384.

DOCUMENTS INCORPORATED BY REFERENCE

None.

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21st Century Holding Company

PART I

SPECIAL NOTE ABOUT FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Report on Form 10-K, other than purely historical information, including estimates, projections, statements relating to our business plans, objectives and expected operating results, and the assumptions upon which those statements are based, are "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements generally are identified by words "believes," "project," "expects," "anticipates," "estimates," "intends," "strategy," "plan," "may," "will," "would," "will be," "will continue," "will likely resu expressions. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties which may cause actual results to differ materially from the forward-looking statements. A detailed discussion of these and other risks and uncertainties that could cause actual results and events to differ materially from such forward-looking statements is included in the section entitled "Risk Factors" in Part I, Item 1A of this Annual Report. We undertake no obligation to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise.

ITEM 1 BUSINESS

GENERAL

21st Century Holding Company ("21st Century", "Company", "we", "us") is an insurance holding company that control substantially all steps in the insurance underwriting, distribution and claims processes through our subsidiaries and our contractual relationships with our independent agents and general agents.

We are authorized to underwrite, and/or place through our wholly owned subsidiaries, homeowners' multi-peril ("homeowners"), commercial general liability, personal and commercial automobile, personal umbrella, fire, allied lines, workers' compensation and commercial inland marine insurance in Florida and various other states. We market and distribute our own and third-party insurers' products and our other services through a network of independent agents. We also utilize a select number of general agents for the same purpose.

• Our primary insurance subsidiary is Federated National Insurance Company ("Federated National"). Federated National is licensed as an admitted carrier in Florida. An admitted carrier is an insurance company that has received a license from the state department of insurance giving the company the authority to write specific lines of insurance in that state. Through contractual relationships with a network of approximately 3,000 independent agents, of which approximately 600 actively sell and service our products, Federated National is authorized to underwrite homeowners', fire, allied lines and personal and commercial automobile insurance in Florida. Federated National is also licensed as an admitted carrier in Alabama, Louisiana, Georgia and Texas, and underwrites commercial general liability insurance in those states. Federated National operated as a non-admitted carrier in Arkansas, California, Kentucky, Maryland, Missouri, Nevada, Oklahoma, South Carolina, Tennessee and Virginia, and could underwrite commercial general liability insurance in all of these states. A non-admitted carrier is allowed to do business in that state and is strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud. Sometimes, non-admitted carriers are referred to as "excess and surplus" lines carriers. Non-admitted carriers are subject to considerably less regulation with respect to policy rates and forms. Non-admitted carriers are not required to financially contribute to and benefit from the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due their policyholders.

In January 2011, we merged Federated National and our other wholly owned insurance subsidiary, American Vehicle Insurance Company (“American Vehicle”), with Federated National continuing the operations of both entities. In connection with this merger, the Company, Federated National and American Vehicle entered into a Consent Order with the Florida Office of Insurance Regulation (“Florida OIR“) pursuant to which we agreed to certain restrictions on our business operations. See “Regulation– Consent Order.”

- We internally process claims made by our insureds through our wholly owned claims adjusting company, Superior Adjusting, Inc. (“Superior”). Until June 2011, we offered premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium Finance, Inc. (“Federated Premium”).

- Assurance Managing General Agents (“Assurance MGA“), a wholly owned subsidiary of the Company, acts as Federated National’s exclusive managing general agent in Florida and is also licensed as a managing general agent in the States of Alabama, Georgia, Illinois, Louisiana, North Carolina, Mississippi, Missouri, New York, Nevada, South Carolina, Texas and Virginia. Assurance MGA has contracted with several unaffiliated insurance companies to sell commercial general liability, workers compensation, personal umbrella and inland marine insurance through Assurance MGA’s existing network of agents.

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Assurance MGA earns commissions and fees for providing policy administration, marketing, accounting and analytical services, and for participating in the negotiation of reinsurance contracts. Assurance MGA earns a $25 per policy fee, and traditionally a 6% commission fee from its affiliates Federated National and American Vehicle. During the fourth quarter of 2010, Assurance MGA, pursuant to the Consent Order as discussed in “Regulation – Consent Order” reduced its fee, to earn amounts varying between 2% and 4%, which we anticipate will return to 6% at an unknown future date with approval from the Florida OIR. A formal agreement reflecting this fee modification was executed during January 2011.

Although we are authorized to underwrite the various lines described above, our business is primarily underwriting homeowners’ policies. During 2011, 81.8%, 10.3%, 4.6% and 3.3% of the premiums we underwrote were for homeowners’, commercial general liability, federal flood, and personal automobile insurance, respectively. During 2010, 79.7%, 12.3%, 4.1% and 3.9% of the premiums we underwrote were for homeowners’, commercial general liability, federal flood, and personal automobile insurance, respectively.

During the years ended December 31, 2011, 2010 or 2009, we did not experience any weather-related catastrophic events such as the hurricanes that occurred in Florida during 2005 and 2004. We are not able to predict how hurricanes or other insurable events will affect our future results of operations and liquidity. Loss and loss adjustment expenses (“LAE”) are affected by a number of factors, many of which are partially or entirely beyond our control, including the following.

- the nature and severity of the loss;
- weather-related patterns;
- the availability, cost and terms of reinsurance;
- underlying settlement costs, including medical and legal costs;
- legal and political factors such as legislative initiatives and public opinion;
- macroeconomic issues.

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 us. When our estimated liabilities for unpaid losses and LAE are less than the actuarially determined amounts, we increase the expense in the current period. Conversely, when our estimated liabilities for unpaid losses and LAE are greater than the actuarially determined amounts, we decrease the expense in the current period.

Our goal in our reinsurance strategy is to equalize the liquidity requirements imposed by most severe insurable events and by all other insurable events we manage in the normal course of business. Please see “Reinsurance Agreements” under “Item 1. Business” for a more detailed description of our reinsurance agreements and strategy.

From time to time, new regulations and legislation are proposed to limit damage awards, to control plaintiffs' counsel fees, to bring the industry under regulation by the Federal government, to control premiums, policy terminations and other policy terms and to impose new taxes and assessments. It is not possible to predict whether, in what form or in what jurisdictions, any of these proposals might be adopted, or the effect, if any, on us.

Our executive offices are located at 14050 N.W. 14th Street, Suite 180, Sunrise, Florida 33323 and our telephone number is (954) 581-9993.

Our internet web sites are www.21stcenturyholding.com, primarily for investors and myFNIC.com, primarily for policy holders and agents. Our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form

8-K and amendments to such reports are available, free of charge, through our website as soon as reasonably practicable after we electronically file or furnish such material to the Securities and Exchange Commission ("SEC"). Further, a copy of this annual report on Form 10-K is located at the SEC's Public Reference Room at 100 F Street, NE, Washington, D.C. 20549. Information on the operation of the Public Reference Room can be obtained by calling the SEC at 1-800-SEC-0330. The SEC maintains an internet site that contains reports, proxy and information statements and other information regarding our filings at www.sec.gov.

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RECENT DEVELOPMENTS

In February 2012, we received approval from the Florida OIR of a 14.1% rate increase. That rate increase, together with our 2011 rate increases for our voluntary property book of homeowners' business, averaging 20.2% statewide, and our assumed property book of homeowners' business, averaging 13.9% statewide, are expected to gain momentum and accrete throughout 2012.

The Company anticipates unfavorable pricing terms on our upcoming reinsurance contracts due to reduced Florida Hurricane Catastrophe Fund ("FHCF") capacity, though we also anticipate that this higher marginal rate will be mitigated by a reduced reinsurance requirement.

BUSINESS STRATEGY

We expect that in 2012 we will capitalize on our operational efficiencies and business practices through:

- improved property analytical qualities such as a broader geographical dispersion of risks throughout the state of Florida and avoiding risks that do not yield an underwriting profit;
- continued territorial expansion of our commercial general liability, inland marine, and private passenger automobile insurance products into additional states;
- employing our business practices developed and used in Florida in our expansion to other selected states;
- maintaining a commitment to provide high quality customer service to our agents and insureds;
- expansion of our marketing efforts by retaining key personnel and implementing direct marketing technologies;
- offering attractive incentives to our agents to place a high volume of quality business with our companies;
- offering our employees continuing education classes appropriate to the respective discipline employed within this organization;
- assumption of existing risks from other carriers; and
- additional strategies that may include possible acquisitions or further dispositions of assets, and development of procedures to improve claims history and mitigate losses from claims.

There can be no assurances, however, that any of the foregoing strategies will be developed or successfully implemented or, if implemented, that they will positively affect our results of operations.

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INSURANCE OPERATIONS AND RELATED SERVICES

Overview of Insurance Lines of Business

The following tables set forth the amount and percentages of our consolidated gross premiums written, premiums ceded to reinsurers and net premiums written by line of business for the periods indicated.

	Years Ended December 31,					
	2011		2010		2009	
	Premium	Percent	Premium	Percent	Premium	Percent
	(Dollars in Thousands)					
Gross written premiums:						
Automobile	$3,274	3.3 %	$3,721	3.9 %	$836	0.8 %
Federal Flood	4,468	4.5 %	3,951	4.1 %	3,559	3.4 %
Homeowners'	80,403	81.9 %	76,845	79.7 %	84,705	81.2 %
Commercial General Liability	10,125	10.3 %	11,894	12.3 %	15,279	14.6 %
Total gross written premiums	$98,270	100.0 %	$96,411	100.0 %	$104,379	100.0 %
Ceded premiums:						
Automobile	$1,541	3.3 %	$1,882	3.6 %	$14	0.0 %
Federal Flood	4,468	9.7 %	3,951	7.5 %	3,559	6.3 %
Homeowners'	40,273	87.0 %	46,893	88.5 %	52,518	93.5 %
Commercial General Liability	12	0.0 %	238	0.4 %	126	0.2 %
Total ceded premiums	$46,294	100.0 %	$52,964	100.0 %	$56,217	100.0 %
Net written premiums						
Automobile	$1,733	3.3 %	$1,839	4.3 %	$822	1.7 %
Federal Flood	-	0.0 %	-	0.0 %	-	0.0 %
Homeowners'	40,130	77.2 %	29,952	68.9 %	32,187	66.8 %
Commercial General Liability	10,113	19.5 %	11,656	26.8 %	15,153	31.5 %
Total net written premiums	$51,976	100.0 %	$43,447	100.0 %	$48,162	100.0 %

Homeowners' Property and Casualty Insurance

Federated National underwrites homeowners' insurance primarily in the South, West and Central Florida regions. Homeowners' insurance generally protects an owner of real and personal property against covered causes of loss to that property. The table that follows reflects the number of homeowner policies in-force by South Florida counties and all other Florida counties and reflects our concentrations of risk from catastrophic events.

	In-Force Policy Count					
	Years Ended December 31,					
	2011		2010		2009	
County	Amount	Percentage	Amount	Percentage	Amount	Percentage
Dade	1,944	4.4 %	2,835	6.6 %	3,544	6.7 %
Broward	4,386	10.0 %	5,008	11.6 %	4,139	7.9 %
Pinellas	3,788	8.6 %	3,437	8.0 %	5,147	9.8 %

Hillsborough	2,984	6.8	%	3,265	7.6	%	4,505	8.6	%
West Palm Beach	8,203	18.7	%	12,221	28.3	%	14,543	27.6	%
All others	22,488	51.5	%	16,366	37.9	%	20,728	39.4	%
Total	43,793	100.0	%	43,132	100.0	%	52,606	100.0	%

(a) immaterial amounts are included in "All Others"

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Our homeowner insurance products provide maximum dwelling coverage in the amount of approximately $1.8 million, with the aggregate maximum policy limit being approximately $3.0 million. We continually subject these limits to review; though there were no material changes during 2011. The approximate average premium on the policies currently in-force is $1,793, as compared with $1,803 for 2010. The typical deductible is either $2,500 or $1,000 for non-hurricane-related claims and generally 2% of the coverage amount for the structure for hurricane-related claims.

Premium rates charged to our homeowner insurance policyholders are continually evaluated to assure that they meet the expectation that they are actuarially sound and produce a reasonable level of profit (neither excessive nor inadequate). Premium rates are regulated and approved by the Florida OIR. Our 14.9% rate increase in connection with our Citizens Property Insurance Corporation (“Citizens”) assumptions was approved during 2010 by the Florida OIR. Additionally, the Florida OIR approved a second 14.1% rate increase in February 2012.

For a further discussion regarding Homeowners’ Property and Casualty Insurance, see “Recent Developments”, above.

Commercial General Liability

We underwrite commercial general liability insurance for approximately 380 classes of artisan (excluding home-builders and developers) and mercantile trades (such as owners, landlords and tenants). The limits of liability range from $100,000 per occurrence with a $200,000 policy aggregate to $1.0 million per occurrence with a $2.0 million policy aggregate. We continually subject these limits to review, though there were no changes during 2011. We market the commercial general liability insurance products through independent agents and a limited number of general agencies unaffiliated with the Company. The average annual premium on policies currently in-force during 2011 is approximately $712, as compared with $734 in 2010.

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

	Years Ended December 31,								
	2011			2010			2009		
	Amount	Percentage		Amount	Percentage		Amount	Percentage	
	(Dollars in Thousands)								
State									
Alabama	$57	0.56	%	$46	0.39	%	$76	0.50	%
Arkansas	-	0.00	%	1	0.01	%	4	0.03	%
California	8	0.08	%	34	0.29	%	49	0.32	%
Florida	8,606	84.99	%	9,972	83.85	%	12,341	80.77	%
Georgia	-	0.00	%	68	0.57	%	291	1.91	%
Kentucky	-	0.00	%	-	0.00	%	1	0.00	%
Louisiana	916	9.05	%	1,094	9.19	%	1,736	11.36	%
Maryland	-	0.00	%	9	0.07	%	-	0.00	%
Oklahoma	2	0.02	%	-	0.00	%	-	0.00	%
South Carolina	2	0.02	%	1	0.01	%	2	0.01	%
Texas	534	5.28	%	665	5.59	%	778	5.09	%
Virginia	-	0.00	%	4	0.03	%	1	0.01	%
Total	$10,125	100.00	%	$11,894	100.00	%	$15,279	100.00	%

Personal Automobile

Personal automobile insurance markets can be divided into two categories, standard automobile and nonstandard automobile. Standard personal automobile insurance is principally provided to insureds who present an average risk profile in terms of driving record, vehicle type and other factors. Nonstandard personal automobile insurance is principally provided to insureds that are unable to obtain standard insurance coverage because of their driving record, age, vehicle type or other factors, including market conditions. The average annual nonstandard personal automobile insurance policy currently in-force is approximately $1,104, as compared with $1,007 for 2010, and the nonstandard personal automobile insurance lines represents 100% of our written premiums for personal automobile insurance in 2011 and 2010.

The maximum exposures for the nonstandard policy in Florida are $10,000 per individual, $20,000 per accident for bodily injury, $10,000 per accident for property damage, and predominantly $50,000 for comprehensive and collision. Beginning in late 2010 we underwrote nonstandard personal automobile insurance in Georgia, where the maximum exposures are $25,000 per individual, $50,000 per accident for bodily injury, $25,000 per accident for property damage, and predominantly $50,000 for comprehensive and collision. In addition, we write commercial automobile insurance in Florida. The maximum exposure is predominantly $30,000 on a combined single limit basis.

Flood

Federated National writes flood insurance through the National Flood Insurance Program (“NFIP”). We write the policy for the NFIP, which assumes 100% of the flood risk while we retain a commission for our service. The average flood policy premium is approximately $496 with limits up to $250,000. Commissions in connection with this program totaled $0.2 million in 2011, 2010 and 2009, respectively. Pursuant to the Florida OIR regulations, we are required to report write-your-own-flood premiums on a direct and ceded basis for 2008 and subsequent years. Prior to 2008, we reported only the commissions income associated with this program.

Managing General Agent Services

Assurance MGA, a wholly owned subsidiary of the Company, acts as Federated National’s exclusive managing general agent in Florida and is also licensed as a managing general agent in the States of Alabama, Georgia, Illinois, Louisiana, North Carolina, Mississippi, Missouri, New York, Nevada, South Carolina, Texas and Virginia. Assurance MGA has contracted with several unaffiliated insurance companies to sell commercial general liability, workers compensation, personal umbrella and inland marine insurance through Assurance MGA’s existing network of agents.

Assurance MGA earns commissions and fees for providing policy administration, marketing, accounting and analytical services, and for participating in the negotiation of reinsurance contracts. Assurance MGA earns a $25 per policy fee, and traditionally a 6% commission fee from its affiliates Federated National and American Vehicle. During the fourth quarter of 2010, Assurance MGA, pursuant to the Consent Order as discussed in “Regulation – Consent Order” reduced its fee, to earn amounts varying between 2% and 4%, which we anticipate will return to 6% at an unknown future date with approval from the Florida OIR. A formal agreement reflecting this fee modification was executed during January 2011.

Claims Adjusting

We internally process claims made by our insureds through our wholly owned claims adjusting company, Superior. Our agents have no authority to settle claims or otherwise exercise control over the claims process. Furthermore, we believe that the retention of independent adjusters, in addition to the employment of salaried claims personnel, results in reduced ultimate loss payments, lower LAE and improved customer service for our claimants and policyholders. We also employ an in-house legal department to cost-effectively manage claims-related litigation and to monitor our claims handling practices for efficiency and regulatory compliance.

Premium Finance

Until June 2011, our wholly owned subsidiary, Federated Premium, offered premium financing to our own and third-party insureds. Premium financing has been marketed through our distribution network of general agents and independent agents.

Finance contracts receivable totaled less than $0.1 million as of December 31, 2011, compared with $0.3 million as of December 31, 2010.

The Company anticipates continued use of the direct bill feature associated with our homeowners', commercial general liability and automobile programs. Direct billing is when the insurance company accepts from the insured, as a receivable, a promise to pay the premium, as opposed to requiring payment of the full amount of the policy. The advantage of direct billing a policyholder by the insurance company is that we are not reliant on a credit facility, but remain able to charge and collect interest from the policyholder. We believe that the direct billing program does not increase our risk because the insurance policy, which serves as collateral, is managed by our computer system. Underwriting criteria are designed with down payment requirements and monthly payments that create policyholder equity in the insurance policy. The equity in the policy is collateral for the extension of credit to the insured.

Through our monitoring systems, we track delinquent payments and, in accordance with the terms of the extension of credit, cancel if payment is not made. If any excess premium remains after cancellation of the policy and deduction of applicable penalties, this excess is refunded to the policyholder. The direct bill program enables us to closely manage our risk while providing credit to our insureds.

Independent Insurance Agency

Insure-Link, Inc. ("Insure-Link") was formed in March 2008 to serve as an independent insurance agency. The insurance agency markets direct to the public to provide a variety of insurance products and services to individual clients, as well as business clients, by offering a full line of insurance products including, but not limited to, homeowners', flood, personal and commercial automobile, commercial general liability and workers' compensation insurance through their agency appointments with over fifty different carriers.

MARKETING AND DISTRIBUTION

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

Our independent agents and general agents have the authority to sell and bind insurance coverage in accordance with procedures established by Assurance MGA. Assurance MGA reviews all coverage bound by the agents promptly and generally accepts all coverage that falls within stated underwriting criteria. For all policies issued, Assurance MGA also has the right, within a period that varies by state between 60 days and 120 days from a policy's inception, to cancel any policy, upon an advanced notice provided in accordance with statutory specific guidelines, even if the risk falls within our underwriting criteria.

We believe that our integrated computer systems, which allow for rapid automated premium quotation and policy issuance by our agents, is a key element in providing quality service to both our agents and insureds for various lines of our business.

We believe that the management of our distribution system now centers on our ability to capture and maintain relevant data by producing agents. We believe that information management of agent production, coupled with loss experience, will enable us to maximize profitability.

REINSURANCE AGREEMENTS

Financing risk generally involves a combination of risk retention and risk transfer techniques. "Retention", similar to a deductible, involves financing losses by funds internally generated. "Transfer" involves the existence of a contractual arrangement designed to shift financial responsibility to another party in exchange for premium. Secondary to the primary risk-transfer agreements we use reinsurance agreements to transfer a portion of the risks insured under our policies to other companies through the purchase of reinsurance. We utilize reinsurance to reduce exposure to catastrophic and non-catastrophic risks and to help manage the cost of capital. Reinsurance techniques are designed to lessen earnings volatility, improve shareholder return, and to support the required statutory surplus requirements. We also use reinsurance to realize an arbitrage of premium rates, benefit from the availability of our reinsurers' expertise, and benefit from the management of a profitable portfolio of insureds by way of enhanced analytical capacities.

In addition to reinsurance agreements, we also from time to time enter into retro-cessionary reinsurance agreements; each designed to shift financial responsibility based on predefined conditions. Generally, there are three separate kinds of reinsurance structures – quota share, excess of loss, and facultative, each considered either proportional or non-proportional. Our reinsurance structures are maintained to protect our insurance subsidiary against the severity of losses on individual claims or unusually serious occurrences in which the frequency and or the severity of claims produce an aggregate extraordinary loss from catastrophic events.

Although reinsurance does not discharge us from our primary obligation to pay for losses insured under the policies we issue, reinsurance does make the assuming reinsurer liable to the insurance subsidiary for the reinsured portion of the risk. A credit risk exposure exists with respect to ceded losses to the extent that any reinsurer is unable or unwilling to meet the obligations assumed under the reinsurance contracts. The collectability of reinsurance is subject to the solvency of the reinsurers, interpretation of contract language and other factors. A reinsurer's insolvency or inability to make payments under the terms of a reinsurance contract could have a material adverse effect on our results of operations and financial condition. Our reinsurance structure has significant risks, including the fact that the FHCF may not be able to raise sufficient money to pay its claims or impair its ability to pay its claims in a timely manner. This could result in significant financial, legal and operational challenges to all property and casualty companies associated with FHCF, including our company.

The availability and costs associated with the acquisition of reinsurance will vary year to year. These fluctuations, which can be significant, are not subject to our control and may limit our ability to purchase adequate coverage. For example, FHCF has restricted its very affordable reinsurance capacity for the 2011–2012 and 2010–2011 hurricane seasons and is expected to continue constricting its claim paying capacity for future seasons. This gradual restriction is requiring us to replace that capacity with more expensive private market reinsurance. The recovery of increased reinsurance costs through rate action is not immediate and cannot be presumed, as it is subject to Florida OIR approval. Our reinsurance program is subject to approval by the Florida OIR and review by Demotech, Inc. (“Demotech”).

Our property lines of business include homeowners’ and fire. For the 2011–2012 hurricane season, the excess of loss and FHCF treaties will insure the property lines for approximately $298.0 million of aggregate catastrophic losses and LAE with a maximum single event coverage totaling approximately $226.0 million, with the Company retaining the first $7.0 million of losses and LAE for each event. Our reinsurance program includes coverage purchased from the private market, which affords optional reinstatement premium protection that provides coverage beyond the first event, along with any remaining coverage from the FHCF. Coverage afforded by the FHCF totals approximately $154.1 million, or 51.7% of the $298.0 million of aggregate catastrophic losses and LAE. The FHCF affords coverage for the entire season, subject to maximum payouts, without regard to any particular insurable event.

The estimated cost to the Company for the excess of loss reinsurance products for the 2011-2012 hurricane season, inclusive of approximately $11.7 million payable to the FHCF and the prepaid automatic premium reinstatement protection, is approximately $39.7 million.

Annually, the cost and amounts of reinsurance are based on management's analysis of Federated National's exposure to catastrophic risk as of June 30 and estimated to September 30. Our data is then subjected to actual exposure level analysis as of September 30. This analysis of our exposure level in relation to the total exposures to the FHCF and excess of loss treaties may produce changes in limits and reinsurance premiums as a result of the reconciliation of estimated to actual exposure level. Last year, the September 30, 2010 change to total limits was an increase of $10.3 million of probable maximum loss or 2.9% and the change to reinsurance premiums was an increase of $3.7 million or 8.7%. The September 30, 2011 change to total limits was an increase of $172.2 million of total insured value or 1.4 % and the change to reinsurance premiums was an increase of $0.5 million or 1.1%. The subsequent change to management’s June 30, 2011 exposure analysis, as of September 30, 2011 is being amortized over the underlying policy term.

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The 2011-2012 private reinsurance companies and their respective A.M. Best Company ("A.M. BEST") rating are listed in the table as follows.

Reinsurer	A.M. Best Rating		
UNITED STATES			
American Agricultural Insurance	A-		
Everest Reinsurance Company	A+		(2)
Houston Casualty Co. (UK Branch)	A+		(2)
Munich Reinsurance America, Inc.	A+		(2)
Odyssey Reinsurance Company	A		
QBE Reinsurance Corporation	A		(2)
BERMUDA			
ACE Tempest Reinsurance Ltd.	A+	*	(2)
Arch Reinsurance Limited	A		(2)
Ariel Reinsurance Company Limited	A-	*	
DaVinci Reinsurance Limited	A	*	(2)
D.E. Shaw Re (Bermuda) Ltd.	NR		(1)
JC Re Ltd (Juniperus)	NR	*	(1)
Montpelier Reinsurance Ltd.	A-		
Renaissance Reinsurance Limited	A+	*	(2)
Torus Insurance (Bermuda) Limited	A-	*	
UNITED KINGDOM			
Amlin Syndicate No. 2001 (AML)	A	*	(2)
Antares Syndicate No. 1274 (AUL)	A		(2)
Arrow Syndicate No. 1910 (ARW)	A	*	(2)
Broadgate Underwriting Limited Syndicate No. 1301 (BGT)	A		(2)
Liberty Syndicates Paris/Syndicate 4472	A		(2)
MAP Underwriting Syndicate No. 2791 (MAP)	A	*	(2)
Novae Syndicate No. 2007 (NVA)	A		(2)
EUROPE			
Amlin Bermuda Limited	A		(2)
Flagstone Reassurance Suisse SA	A-		
Lansforsakringar Sak Forsakringsaktiebolag	NR-5		(2)
Scor Switzerland AG	A		(2)

* Reinstatement Premium Protection Program Participants

(1) Participant will fund a trust agreement for their exposure with cash and U.S. Government obligations of American institutions at fair market value.

(2) Standard & Poor's rated "A" or higher (investment grade - economic situation can affect finance)

For the 2010-2011 hurricane season, the excess of loss and FHCF treaties insured the property lines for approximately $360.7 million of aggregate catastrophic losses and LAE with a maximum single event coverage totaling approximately $285.5 million, with the Company retaining the first $5.0 million of losses and LAE for each event. Our reinsurance program included coverage purchased from the private market, which afforded optional reinstatement premium protection that provided coverage beyond the first event, along with coverage from the FHCF. Coverage afforded by the FHCF totaled approximately $220.4 million, or 61.1% of the $360.7 million of aggregate catastrophic losses and LAE. The FHCF affords coverage for the entire season, subject to maximum payouts, without regard to any particular insurable event.

The estimated cost to the Company for the excess of loss reinsurance products for the 2010-2011 hurricane season, inclusive of approximately $19.1 million payable to the FHCF and the prepaid automatic premium reinstatement protection, was approximately $46.5 million.

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21st Century Holding Company

The 2010-2011 private reinsurance companies and their respective A.M. Best rating are listed in the table as follows.

Reinsurer	A.M. Best Rating		
UNITED STATES			
American Agricultural Insurance	A		(2)
Everest Reinsurance Company	A+		(2)
Munich Reinsurance America, Inc.	A+		(2)
QBE Reinsurance Corporation	A		(2)
BERMUDA			
ACE Tempest Reinsurance Ltd.	A+	*	(2)
Actua Re Limited	NR	*	(1)
Amlin Bermuda Limited	A		(2)
Ariel Reinsurance Company Limited	A-	*	
DaVinci Reinsurance Limited	A	*	(2)
Flagstone Reinsurance Limited	A-		
Montpelier Reinsurance Ltd.	A-		(2)
Nephila/ Allianz Risk Trnsfr Zurich (BDA)	NR-5	*	(2)
Renaissance Reinsurance Limited	A+	*	(2)
Torus Insurance (Bermuda) Limited	A-	*	
UNITED KINGDOM			
Antares Syndicate No. 1274 (AUL)	A		(2)
Broadgate Underwriting Limited Syndicate No. 1301 (BGT)	A		(2)
Arrow Syndicate No. 1910 (ARW)	A	*	(2)
Amlin Syndicate No. 2001 (AML)	A		(2)
Novae Syndicate No. 2007 (NVA)	A		(2)
Houson Casualty Co. (UK Branch)	A+		(2)
EUROPE			
Lansforsakringar Sak Forsakringsaktiebolag	NR-5		(2)
Liberty Syndicates Paris/Syndicate 4472	A		(2)

* Reinstatement Premium Protection Program Participants

(1) Participant has funded a trust agreement for their exposure with approximately $3.8 million of cash and U.S. Government obligations of American institutions at fair market value.

(2) Standard & Poor's rated "A" or higher (investment grade - economic situation can affect finance)

For the 2012-2013 hurricane season, Federated National entered into a Reimbursement Contract and Addendum No. 1 thereto with SBA on February 28, 2012. This Reimbursement Contract will reimburse Federated National for covered property losses under its homeowners' insurance policies resulting from hurricanes that cause damage in the State of Florida through May 31, 2013. Under this Reimbursement Contract, the FHCF will provide approximately $135.0 million of aggregate seasonal coverage for covered losses in excess of approximately $53.0 million, subject to a

10.0% Company participation. Federated National's premium for the FHCF reinsurance coverage will be approximately $8.2 million payable in three installments between August 2012 and December 2012. The actual attachment point, total coverage and cost will not be finalized until December 31, 2012.

Pursuant to commutation provisions contained in the original 2005 FHCF agreement, on July 21, 2011 Federated National and the FHCF negotiated such a commutation agreement for the 2005 contract year. The terms of the agreement provide that Federated National release the FHCF from all its obligations under the original reinsurance agreement for a negotiated consideration as a final payment for all unpaid claims subject to the treaty. This negotiation resulted in a final commutation payment received by us for a total of $4.1 million, which is the maximum available under the treaty to pay loss and LAE including incurred but not yet reported ("IBNR") for the subject losses. The benefit of the FHCF treaty inures to the benefit of the private reinsurers participating in the treaty.

As a direct premium writer in the state of Florida, we are required to participate in certain insurer solvency associations under Florida Statutes Section 631.57(3) (a), administered by the Florida Insurance Guaranty Association ("FIGA"). Participation in these pools is based on our written premium by line of business to total premiums written statewide by all insurers. Participation has resulted in assessments against us, as it had in 2006 and 2007, and again on October 30, 2009. There were no assessments made during the years ended December 31, 2008, 2010 or 2011. Through 2007, we were assessed $6.6 million and in 2009 we were assessed an additional $0.6 million in connection with the insolvencies of domestic insurance companies. For statutory accounting these assessments were not charged to operations, in contrast, Generally Accepted Accounting Principles ("GAAP") treatment was to charge current operations for the assessments. If new assessments occur, we will be required to treat these assessments consistent with GAAP since accounting difference with Statutory accounting no longer exists as of January 1, 2011. Through policyholder surcharges, as approved by the Florida OIR, we have since fully recouped $7.2 million in connection with these assessments.

Related to statutory accounting, in October 2010, the National Association of Insurance Commissioners ("NAIC") issued substantive revisions in SSAP No. 35R, Guaranty Fund and Other Assessments. For statutory accounting, SSAP No. 35R, effective January 1, 2011, requires assessments that could be recouped through future premium surcharges be expensed and an asset cannot be recognized. The impact is there might be an effect on statutory policyholder surplus once the liability for the assessments is recognized. The adoption of SSAP No. 35R rule will not have a material effect on our current operations.

The FHCF reimbursement contract and addendums were all effective June 1, 2011, and the private excess of loss type treaties were all effective July 1, 2011; all treaties have a term of one year. Our reinsurance treaty with the FHCF has a significant credit risk, including the fact that the FHCF may not be able to raise sufficient money to pay its claims or be able to pay its claims in a timely manner. This could result in significant financial, legal and operational challenges to all companies, including ours. Additionally, the FHCF treaty contains an exclusion for “Losses in excess of the sum of the Balance of the Fund as of December 31 of the Contract Year and the amount the SBA is able to raise through the issuance of revenue bonds or by the use of other financing mechanisms, up to the limit pursuant to Section 215.555(4) (c), Florida Statutes.” This credit risk is mitigated by a fund cash buildup due to the absence of covered events in recent years.

To date, we have made no claims asserted against our reinsurers in connection with the 2011–2012 and 2010–2011 excess of loss and FHCF treaties.

As regards to the commercial multi-peril property program that began recording premium on August 28, 2009, we have secured an automatic facultative reinsurance agreement with Munich Reinsurance America, Inc. (“Munich Re”) and Ascot Underwriting Limited (“Ascot”) for bound risks with total insured values not to exceed $10.0 million, with additional coverage in excess of $10.0 million available upon submission and subjected to underwriting guidelines. This coverage excludes catastrophic wind-storm risk. A.M. Best ratings for Munich Re and Ascot are A+ and A, respectively.

During 2010, the Company secured casualty reinsurance affording coverage totaling $4.0 million in excess of $1.0 million. This reinsurance also protects the Company against extra contractual obligations and losses in excess of policy limits. Any loss occurrence that involves liability exposure written by either Federated National or American Vehicle or a combination of both will be covered. The cost of this coverage totaled approximately $0.5 million.

In order to expand our commercial business, American Vehicle entered into various quota share reinsurance agreements whereby American Vehicle is the assuming reinsurer. On March 26, 2009, we announced that American

Vehicle received approval from the Florida OIR to enter into a reinsurance relationship allowing the opportunity to market and underwrite commercial insurance through a company that has an "A" rating with A.M. Best. This agreement was designed to enable the deployment of commercial general liability and other commercial insurance products in most of the contiguous 48 states to policyholders who require their commercial insurance policy to come from an insurance company with an A- or better A.M. Best rating. Operations began during the quarter ended June 30, 2009. During 2011, the companies mutually agreed to suspend this treaty effective May 15, 2011.

The quota share retrocessionaire reinsurance agreements require American Vehicle to securitize credit, regulatory and business risk. As of December 31, 2010, irrevocable letters of credit fully collateralized by American Vehicle and further guaranteed by the parent company, 21st Century, were replaced by fully funded trust agreements. Fully funded trust agreements totaled $4.7 million and $4.6 million as of December 31, 2011 and December 31, 2010, respectively.

LIABILITY FOR UNPAID LOSSES AND LAE

We are directly liable for loss and LAE payments under the terms of the insurance policies that we write. In many cases, there may be a time lag between the occurrence and reporting of an insured loss and our payment of that loss. As required by insurance regulations and accounting rules, we reflect the liability for the ultimate payment of all incurred losses and LAE by establishing a liability for those unpaid losses and LAE for both reported and unreported claims, which represent estimates of future amounts needed to pay claims and related expenses.

When a claim, other than personal automobile, involving a probable loss is reported, we establish a liability for the estimated amount of our ultimate losses and LAE payments. The estimate of the amount of the ultimate loss is based upon such factors as the type of loss, jurisdiction of the occurrence, knowledge of the circumstances surrounding the claim, severity of injury or damage, potential for ultimate exposure, estimate of liability on the part of the insured, past experience with similar claims and the applicable policy provisions.

All newly reported claims received with respect to personal automobile policies are set up with an initial average liability. The average liability for these claims is determined by dividing the number of reported claims into the total amount paid during the same period. If a claim is open more than 45 days, that open case liability is evaluated and the liability is adjusted upward or downward according to the facts and circumstances of that particular claim.

In addition, management provides for a liability on an aggregate basis to provide for IBNR. We utilize independent actuaries to help establish liability for unpaid losses and LAE. We do not discount the liability for unpaid losses and LAE for financial statement purposes.

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

Among our classes of insurance, the automobile and homeowners' liability claims historically tend to have longer time lapses between the occurrence of the event, the reporting of the claim and the final settlement, than do automobile physical damage and homeowners' property claims. These liability claims often involve parties filing suit and therefore may result in litigation. By comparison, property damage claims tend to be reported in a relatively shorter period of time and settled in a shorter time frame with less occurrence of litigation.

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

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The following table sets forth a reconciliation of beginning and ending liability for unpaid losses and LAE as shown in our consolidated financial statements for the periods indicated.

	Years Ended December 31,		
	2011	2010	2009
	(Dollars in Thousands)		
Balance at January 1	$ 66,529	$ 70,610	$ 64,775
Less reinsurance recoverables	(6,810)	(11,594)	(12,713)
Net balance at January 1	$ 59,719	$ 59,016	$ 52,062
Incurred related to			
Current year	$ 31,893	$ 37,288	$ 41,988
Prior years	(997)	2,800	1,718
Total incurred	$ 30,896	$ 40,088	$ 43,706
Paid related to			
Current year	$ 13,672	$ 15,077	$ 18,478
Prior years	19,048	24,308	18,274
Total paid	$ 32,720	$ 39,385	$ 36,752
Net balance at year-end	$ 57,895	$ 59,719	$ 59,016
Plus reinsurance recoverables	2,088	6,810	11,595
Balance at year-end	$ 59,983	$ 66,529	$ 70,611

As shown above, and as a result of review of liability for losses and LAE, which includes a re-evaluation of the adequacy of reserve levels for prior year's claims, we decreased the liability for losses and LAE for claims occurring in prior years by $1.0 million for the year ended December 31, 2011, and we increased the liability for losses and LAE for claims occurring in prior years by $2.8 million and $1.7 million for the years ended December 31, 2010 and 2009, respectively.

In 2011, we increased incurred losses and LAE for claims in connection with the hurricanes in 2005 and 2004 by approximately $0.2 million and decreased the incurred loss and LAE attributed to incurred events of prior years in connection with our homeowners', automobile and commercial general liability lines of business by $1.5 million.

In 2010, we increased incurred losses and LAE for claims in connection with the hurricanes in 2005 and 2004 by approximately $1.6 million and increased the incurred loss and LAE attributed to incurred events of prior years in connection with our homeowners', automobile and commercial general liability lines of business by $1.2 million.

Based upon discussions with our independent actuarial consultants and their statements of opinion on losses and LAE, we believe that the liability for unpaid losses and LAE is currently adequate to cover all claims and related expenses which may arise from incidents reported and IBNR as of December 31, 2011.There can be no assurance concerning future adjustments of reserves, positive or negative, for claims incurred through December 31, 2011.

The following table presents total unpaid losses and LAE, net, and total reinsurance recoverable, on a run-off basis, due from our automobile reinsurers as shown in our consolidated financial statements for the periods indicated.

	As of December 31,	
	2011	2010
	(Dollars in Thousands)	
Transatlantic Reinsurance Company (A+ A.M. Best rated)		
Reinsurance (payable) recoverable on paid losses and LAE	(23)	$1
Unpaid losses and LAE	$113	38
	$90	$39

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The following table presents total unpaid losses and LAE, net, and total reinsurance recoverable due from our catastrophic reinsurers as shown in our consolidated financial statements.

	As of December 31,	
	2011	2010
Catastrophe Excess of Loss (various participants) and FHCF	(Dollars in Thousands)	
Reinsurance recoverable on paid losses and LAE	$8	$1,542
Unpaid losses and LAE	542	5,514
	$550	$7,056
Amounts due from (to) reinsurers consisted of amounts related to:		
Unpaid losses and LAE	$542	$5,514
Reinsurance recoverable on paid LAE	8	1,542
Reinsurance payable	(1)	(14,088)
	$549	$(7,032)

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The following table presents the Statutory liability for unpaid losses and LAE, net of reinsurance recoverable for the years ended December 31, 2002 through 2011 and does not distinguish between catastrophic and non-catastrophic events. The top line of the table shows the estimated net liabilities for unpaid losses and LAE at the balance sheet date for each of the periods indicated. These figures represent the estimated amount of unpaid losses and LAE for claims arising in all prior years that were unpaid at the balance sheet date, including losses that had been IBNR. The portion of the table labeled "Cumulative paid as of" shows the net cumulative payments for losses and LAE made in succeeding years for losses incurred prior to the balance sheet date. The lower portion of the table shows the re-estimated amount of the previously recorded liability based on experience as of the end of each succeeding year.

Years Ended December 31,
(Dollars in Thousands)

	2011	2010	2009	2008	2007	2006	2005	2004	2003	2002
Statutory unpaid losses and LAE, net	$55,567	$59,655	$59,016	$52,070	$39,551	$27,259	$25,733	$37,390	$15,314	$9,42
Cumulative paid as of:										
One year later		17,863	22,910	17,264	17,019	19,331	25,465	35,114	10,721	8,62
Two years later			32,086	29,985	25,692	27,724	34,073	48,285	12,600	10,4
Three years later				35,367	35,185	33,308	39,739	53,621	13,558	11,0
Four years later					37,921	40,554	44,085	57,653	14,268	11,9
Five years later						41,335	49,339	60,197	14,583	12,3
Six years later							48,875	62,665	15,852	12,5
Seven years later								62,459	16,234	13,7
Eight years later									16,119	13,8
Nine years later										13,6
Re-estimated net liability as of:										
End of year	55,567	59,655	59,016	52,070	39,551	27,259	25,733	37,390	15,314	9,42
		58,895	61,567	52,755	44,361	35,315	35,804	44,293	14,327	9,85

One year later									
Two years later		61,956	57,791	47,682	38,902	41,449	52,160	14,427	9,82
Three years later			58,113	53,026	45,507	45,295	56,479	15,034	10,1
Four years later				53,189	50,980	51,459	59,400	15,941	11,0
Five years later					50,909	55,779	64,080	15,921	11,2
Six years later						55,385	65,638	18,144	11,2
Seven years later							65,916	18,922	13,5
Eight years later								18,632	15,7
Nine years later									14,7
Cumulative redundancy (deficiency)	760	(2,939)	(6,043)	(13,638)	(23,649)	(29,651)	(28,526)	(3,318)	(5,3
Cumulative redundancy (-) deficiency as a % of reserves originally established	1.3 %	-5.0 %	-11.6 %	-50.0 %	-91.9 %	-79.3 %	-186.3 %	-35.2 %	-86.

The cumulative redundancy or deficiency represents the aggregate change in the estimates over all prior years. A deficiency indicates that the latest estimate of the liability for losses and LAE is higher than the liability that was originally estimated and a redundancy indicates that such estimate is lower. It should be emphasized that the table presents a run-off of balance sheet liability for the periods indicated rather than accident or policy loss development for those periods. Therefore, each amount in the table includes the cumulative effects of changes in liability for all prior periods. Conditions and trends that have affected liabilities in the past may not necessarily occur in the future.

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As noted above, we have since experienced a $0.8 million cumulative redundancy in connection with the re-estimation of all losses that occurred in 2010, mainly on our homeowners' losses. Relative to 2009, the cumulative deficiency in connection with the re-estimation of all losses totaled $2.9 million, from which $1.2 million relates to our homeowners' losses, $1.5 million relates to our commercial general liability losses and $0.2 million relates to our automobile losses.

As noted in our Form 10-K for the fiscal year ended December 31, 2010, we experienced a $2.6 million cumulative deficiency in connection with the re-estimation of all loss that occurred in 2009 and a $5.7 million cumulative deficiency in connection with the re-estimation of all loss that occurred in 2008. Relative to the $2.6 million deficiency, homeowner and commercial general liability losses totaled $1.9 million and $0.7 million, respectively. Relative to the $5.7 million deficiency, our homeowner losses totaled $0.3 million, our automobile losses totaled $1.9 million and our commercial general liability losses totaled $3.5 million.

As noted in our Form 10-K for the fiscal year ended December 31, 2009, we experienced a $0.7 million cumulative deficiency in connection with the re-estimation of all loss that occurred in 2008 and a $8.2 million cumulative deficiency in connection with the re-estimation of all loss that occurred in 2007. Relative to the $0.7 million deficiency, our automobile and commercial general liability losses totaled $1.9 million and $0.1 million, respectively, and our homeowner benefit totaled $1.3 million. Relative to the $8.2 million deficiency, our homeowner and commercial general liability losses totaled $5.0 million and $6.4 million, respectively, and our automobile benefit totaled $3.4 million.

The table below sets forth the differences between loss and LAE reserves as disclosed for GAAP basis compared with Statutory Accounting Principles ("SAP") basis of presentation for the years ended 2011, 2010 and 2009.

	Years Ended December 31, (Dollars in Thousands)		
	2011	2010	2009
GAAP basis Loss and LAE reserves	$ 59,983	$ 66,529	$ 70,611
Less unpaid Losses and LAE ceded	2,319	6,810	11,593
Balance Sheet Liability	57,664	59,719	59,018
Add Insurance Apportionment Plan	17	14	12
SAP basis Loss and LAE reserves	$ 57,681	$ 59,733	$ 59,030

The table below sets forth the differences between loss and LAE incurred as disclosed for GAAP basis compared with SAP basis presentation for the years ended 2011, 2010 and 2009.

	Years Ended December 31, (Dollars in Thousands)		
	2011	2010	2009
GAAP basis Loss and LAE incurred	$ 30,896	$ 40,088	$ 43,706
Intercompany adjusting and other expenses	-	8	4,239
Insurance apportionment plan	(726)	(2)	(7)
SAP basis Loss and LAE incurred	$ 30,170	$ 40,094	$ 47,938

Underwriting results of insurance companies are frequently measured by their Combined Ratios. However, investment income, federal income taxes and other non-underwriting income or expense are not reflected in the Combined Ratio. The profitability of property and casualty insurance companies depends on income from underwriting, investment and service operations. Underwriting results are considered profitable when the Combined Ratio is under 100% and unprofitable when the Combined Ratio is over 100%.

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The following table sets forth Loss Ratios, Expense Ratios and Combined Ratios for the periods indicated for the insurance business of Federated National and American Vehicle for 2011, 2010 and 2009, and are inclusive of Unallocated Loss Adjustment Expenses ("ULAE").

	Years Ended December 31,					
	2011		2010		2009	
Loss Ratio	63.7	%	89.0	%	91.1	%
Expense Ratio	58.2	%	74.7	%	65.1	%
Combined Ratio	121.9	%	163.7	%	156.2	%

COMPETITION

We operate in highly competitive markets and face competition from national, regional and residual market insurance companies in the homeowners', commercial general liability, and automobile markets. Our competitors include companies that market their products through agents, as well as companies that 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 compete based on underwriting criteria, our distribution network and superior service to our agents and insureds. 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.

In Florida, more than 200 companies are authorized to underwrite homeowners' insurance. Several of our competitors include Citizens, Universal Property and Casualty Insurance Company and St. Johns Insurance Company. In Florida, more than one dozen companies compete with us in commercial general liability insurance market.

Significant competition also emerged because of fundamental changes in 2007 made to the property and casualty insurance business in Florida, which resulted in a multi-pronged approach to address the cost of residential property insurance in Florida. First, the law increased the capacity of reinsurance that stabilized the reinsurance market to the benefit of the insurance companies writing properties lines in Florida. Secondly, the law provided for rate relief to all policyholders. The law also authorized the state-owned insurance company, Citizens, which is free of many of the restraints on private carriers such as surplus, ratios, income taxes and reinsurance expense, to reduce its premium rates and begin competing against private insurers in the residential property insurance market and expands the authority of Citizens to write commercial insurance.

REGULATION

General

We are subject to the laws and regulations in Alabama, Florida, Georgia, Illinois, Kentucky, Louisiana, Maryland, Mississippi, Missouri, New York, Nevada, North Carolina, Ohio, Oklahoma, South Carolina, Tennessee, Texas and Virginia and regulations of any other states in which we seek to conduct business in the future. The regulations cover all aspects of our business and are generally designed to protect the interests of insurance policyholders, as opposed to the interests of shareholders. Such regulations relate to authorized lines of business, capital and surplus requirements, allowable rates and forms, investment parameters, underwriting limitations, transactions with affiliates, dividend limitations, changes in control, market conduct, maximum amount allowable for premium financing service charges and a variety of other financial and non-financial components of our business. Our failure to comply with certain provisions of applicable insurance laws and regulations could have a material adverse effect on our business, results of

operations or financial condition. In addition, any changes in such laws and regulations, including the adoption of consumer initiatives regarding rates charged for coverage, could materially and adversely affect our operations or our ability to expand.

The impact of the Florida legislation enacted after the 2004 and 2005 Florida hurricane seasons that froze premium rates to 2007 levels continues to unwind. That legislation, among other things, provided low cost reinsurance to member insurance companies, accelerated rate filings to reflect the reduced reinsurance costs and expanded the role of Citizens in the market place. Other provisions contained in the emergency rule prevented non-renewals and cancellation (except for material misrepresentation and non-payment of premium) and new restrictions on coverage are prohibited. We estimate that with the recently approved rate increases, our property rates have effectively returned to 2007 pre-legislative levels.

Most states' laws restrict an insurer's underwriting discretion, such as the ability to terminate policies, terminate agents or reject insurance coverage applications, and many state regulators have the power to reduce, or to disallow, increases in premium rates. In addition, state laws generally require that rate schedules and other information be filed with the state's insurance regulatory authority, either directly or through a rating organization with which the insurer is affiliated. The regulatory authority may disapprove a rate filing if it finds that the rates are inadequate, excessive or unfairly discriminatory. Rates, which are not necessarily uniform for all insurers, vary by class of business, hazard covered, and size of risk. Certain states, including Florida, as discussed above, have adopted laws or are considering proposed legislation which, among other things, limit the ability of insurance companies to effect rate increases or to cancel, reduce or non-renew insurance coverage with respect to existing policies, particularly personal automobile insurance.

Most states require licensure or regulatory approval prior to the marketing of new insurance products. Typically, licensure review is comprehensive and includes a review of a company's business plan, solvency, reinsurance, character of its officers and directors, rates, forms and other financial and non-financial aspects of a company. The regulatory authorities may prohibit entry into a new market by not granting a license or by withholding approval.

All insurance companies must file quarterly and annual statements with certain regulatory agencies and are subject to regular and special examinations by those agencies. We may be the subject of additional special examinations or analysis. These examinations or analysis may result in one or more corrective orders being issued by the Florida OIR.The most recent balance sheet audit of Federated National by the Florida OIR occurred as of December 31, 2009. There were no material findings by the independent auditors in connection with this examination. Federated National also experienced a regularly scheduled statutory examination by the Florida OIR which occurred during 2010 for the five years ended December 31, 2009. There were no material findings in connection with this examination.

In some instances, various states routinely require deposits of assets for the protection of policyholders either in those states or for all policyholders. As an example, the Florida OIR requires Federated National to have securities with a fair market value of $2.0 million held in escrow. As of December 31, 2011, Federated National held investment securities with a fair value of approximately $2.1 million, as a deposit with the State of Florida. Additionally, as of December 31, 2011 Federated National had cash deposits totaling $406,400 with the State of Alabama, $151,000 with the State of Arkansas, $118,520 with the State of Louisiana and $25,000 with the State of Georgia.

As of December 31, 2010, Federated National and American Vehicle held investment securities with a fair value of approximately $1.1 million, each as deposits with the State of Florida. Additionally, as of December 31, 2010 American Vehicle had cash deposits totaling $416,400 with the State of Alabama, $160,300 with the State of Arkansas, $118,283 with the State of Louisiana and $25,000 with the State of Georgia.

Consent Order

As part of its approval of the January 2011 merger between Federated National and American Vehicle, the Florida OIR, the Company, Federated National and American Vehicle entered into a consent order with the Florida OIR dated January 25, 2011 (the "Consent Order") pursuant to which the Company and the resulting company in the merger (the "Merged Company") agreed to the following:

- The Merged Company retained the following licenses: (010) Fire, (020) Allied Lines, (040) Homeowners Multi Peril, (050) Commercial Multi Peril, (090) Inland Marine, (170) Other Liability, (192) Private Passenger Auto Liability, (194) Commercial Auto Liability, (211) Private Passenger Auto Physical Damage and (212) Commercial Auto Physical Damage.

- The Merged Company will not write commercial multi peril policy premium without prior approval from the Florida OIR. The Merged Company has no commercial multi peril policy premium in force.

- The Merged Company surrendered its surety license. The Merged Company has no surety policy premium in force.

- The Merged Company will not write new commercial habitation condominium associations without prior approval from the Florida OIR. The current commercial habitation book of business is approximately $1.6 million of policy premium, which will renew pursuant to normal underwriting guidelines.

- The Merged Company agreed to reduce the total number of its homeowners' policies in Miami-Dade, Broward and Palm Beach counties (the "Tri-County Area") to 40% of its entire homeowners' book by December 31, 2011 and limit its new homeowners' policies in the Tri-County Area to $500,000 of new policy premium per month. The 40% was achieved through the increased writing of property located outside of the Tri-County Area, the non-renewal of certain policies located within the Tri-County Area, and limiting the writing of new property located within the Tri-County Area. As of December 31, 2011, the Company had approximately 33.2% of its homeowners' policies located within Tri-County Area.

- The managing general agency fees payable by the Merged Company to Assurance MGA, a wholly owned subsidiary of the Company, which were traditionally 6% of gross written premium, were reduced and will not exceed 4% without prior approval from the Florida OIR. The Merged Company has lowered the fee to 2% of gross written to further support the Federated National's results of operations. This will have no impact on the Company's consolidated financial results.

- The claims service fees payable by the Merged Company to Superior were reduced from the traditional 4.5% of gross earned premium to 3.6% of gross earned premium. This will have no impact on the Company's consolidated financial results.

- The Company provided the Florida OIR with a plan of operation and has agreed to provide certain reports to the Florida OIR on a monthly basis, and agreed to obtain the Florida OIR's approval prior to making any changes to the officers of the Merged Company during the first year following the effective date of the Merger.

Restrictions in Payments of Dividends by Domestic Insurance Companies

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

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

No dividends were paid by Federated National or American Vehicle in 2011, 2010 and 2009, and none are anticipated in 2012 as a result of our Consent Order with the Florida OIR. Although we believe that amounts required to meet our financial and operating obligations will be available from sources other than dividends from our insurance subsidiaries, there can be no assurance in this regard. Further, there can be no assurance that, if requested, the Florida OIR will allow any dividends to be paid by Federated National to us, the parent company, in the future. The maximum dividends permitted by state law are not necessarily indicative of an insurer's actual ability to pay dividends or other distributions to a parent company, which also may be constrained by business and regulatory considerations, such as the impact of dividends on capital surplus, which could affect an insurer's competitive position, the amount of

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

While the non-insurance company subsidiaries (Assurance MGA, Superior and any other affiliate) are not subject directly to the dividend and other distribution limitations, insurance holding company regulations govern the amount that any affiliate within the holding company system may charge any of the insurance companies for service (e.g., management fees and commissions).

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NAIC Risk-Based Capital Requirements

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

Based upon the 2011 and 2010 statutory financial statements for Federated National, statutory surplus exceeded the regulatory action levels established by the NAIC's risk-based capital requirements.

American Vehicle's statutory surplus exceeded the NAIC regulatory action levels in 2010 as well.

Based on risk-based capital requirements, the extent of regulatory intervention and action increases as the ratio of an insurer's statutory surplus to its Authorized Control Level ("ACL"), as calculated under the NAIC's requirements, decreases. The first action level, the Company Action Level, requires an insurer to submit a plan of corrective actions to the insurance regulators if statutory surplus falls below 200.0% of the ACL amount. The second action level, the Regulatory Action Level, requires an insurer to submit a plan containing corrective actions and permits the insurance regulators to perform an examination or other analysis and issue a corrective order if statutory surplus falls below 150.0% of the ACL amount. The third action level, ACL, allows the regulators to rehabilitate or liquidate an insurer in addition to the aforementioned actions if statutory surplus falls below the ACL amount. The fourth action level is the Mandatory Control Level, which requires the regulators to rehabilitate or liquidate the insurer if statutory surplus falls below 70.0% of the ACL amount. Federated National's ratio of statutory surplus to its ACL was 409.7%, 222.8 % and 245.1% at December 31, 2011, 2010 and 2009, respectively. American Vehicle's ratio of statutory surplus to its ACL was 373.4% and 426.9% at December 31, 2010 and 2009, respectively.

NAIC Insurance Regulatory Information Systems ("IRIS") Ratios

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

As of December 31, 2011, Federated National was outside NAIC's usual range for two of thirteen IRIS ratios. These exceptions related to two-years overall operating ratio and investment yield.

As of December 31, 2010, Federated National was outside NAIC's usual range for four of thirteen IRIS ratios. These exceptions related to two-years overall operating ratio, investment yield, gross change in policyholders' surplus and change in adjusted policyholders' surplus. The Florida OIR approved an additional rate increase for our voluntary property book of homeowners' business which averaged 20.2% statewide and went into effect November 1, 2009 and December 1, 2009 for new and renewed homeowner insurance policies, respectively.

As of December 31, 2009, Federated National was outside NAIC's usual range for four of thirteen IRIS ratios. Three exceptions related to underwriting operations and one related to lower than expected investment yields. The operations ratios relate to the timing of premium rate corrections and elevated reinsurance costs. The Florida OIR granted Federated National an average statewide increase of 19.0% for policies that went into effect November 1, 2009 and December 1, 2009 for new and renewed homeowner insurance policies, respectively.

As of December 31, 2010, American Vehicle was outside NAIC's usual range for four of thirteen IRIS ratios. These exceptions related to two-years overall operating ratio, investment yield, gross change in policyholders' surplus and change in adjusted policyholders' surplus.

As of December 31, 2009, American Vehicle was outside NAIC's usual range for three of thirteen IRIS ratios. These ratios reflect the decline in premium volume and operating results. The third ratio related to lower than expected investment yields.

There was no action taken by the Florida OIR in connection with the December 31, 2009 or 2010 IRIS ratio results. We do not currently believe that the Florida OIR will take any significant action with respect to Federated National regarding the 2011 IRIS ratios, although there can be no assurance that will be the case.

Insurance Holding Company Regulation

We, the parent company, are subject to laws governing insurance holding companies in Florida where Federated National is domiciled. These laws, among other things, (i) require us to file periodic information with the Florida OIR, including information concerning our capital structure, ownership, financial condition and general business operations, (ii) regulate certain transactions between us and our affiliates, including the amount of dividends and other distributions, the terms of surplus notes and amounts that our affiliates can charge the holding company for services such as management fees or commissions, (iii) restrict the ability of any one person to acquire certain levels of our voting securities without prior regulatory approval. Any purchaser of 5% or more of the outstanding shares of our Common Stock will be presumed to have acquired control of Federated National unless the Florida OIR, upon application, determines otherwise.

Underwriting and Marketing Restrictions

During the past several years, various regulatory and legislative bodies have adopted or proposed new laws or regulations to address the cyclical nature of the insurance industry, catastrophic events and insurance capacity and pricing. These regulations include (i) the creation of "market assistance plans" under which insurers are induced to provide certain coverages, (ii) restrictions on the ability of insurers to rescind or otherwise cancel certain policies in mid-term, (iii) advance notice requirements or limitations imposed for certain policy non-renewals and (iv) limitations upon or decreases in rates permitted to be charged.

Industry Ratings Services

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

As of December 31, 2011, Federated National is rated by Demotech as "A" ("Exceptional"), which is the third of seven ratings, and defined as “Regardless of the severity of a general economic downturn or deterioration in the insurance cycle, insurers earning a Financial Stability Rating ("FSR") of “A” possess “Exceptional” financial stability related to maintaining surplus as regards to policyholders”. Demotech’s ratings are based upon factors of concern to agents, reinsurers and policyholders and are not primarily directed toward the protection of investors. Our Demotech rating could be jeopardized by factors including adverse development and various surplus related ratio exceptions. On March 16, 2012, Demotech reaffirmed Federated National’s FSR of “A” (“Exceptional”).

The withdrawal of our ratings could limit or prevent us from writing or renewing desirable insurance policies, from competing with insurers who have higher ratings, from obtaining adequate reinsurance, or from borrowing on a line of credit. The withdrawal of our ratings could have a material adverse effect on the Company’s results of operations and financial position because the Company’s insurance products might no longer be acceptable to the secondary marketplace and mortgage lenders. Furthermore, a withdrawal of our ratings could prevent independent agents from

selling and servicing our insurance products.

EMPLOYEES

As of December 31, 2011, we had 112 employees, including two executive officers. We are not a party to any collective bargaining agreement and we have not experienced work stoppages or strikes as a result of labor disputes. We consider relations with our employees to be satisfactory.

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21st Century Holding Company

ITEM 1A RISK FACTORS

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

Risks Related to Our Business

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

We write insurance policies that cover homeowners’, business owners and automobile owners for losses that result from, among other things, catastrophes and sinkholes. Catastrophic losses can be caused by hurricanes, tropical storms, tornadoes, wind, hail, fires, riots and explosions, and their incidence and severity are inherently unpredictable. The extent of losses from a catastrophe is a function of two factors: the total amount of the insurance company's exposure in the area affected by the event and the severity of the event. Our policyholders are currently concentrated in South and Central Florida, which is especially subject to adverse weather conditions such as hurricanes and tropical storms.

The occurrence of claims from catastrophic events could result in substantial volatility in our results of operations or financial condition for any fiscal quarter or year. Increases in the values and concentrations of insured property may also increase the severity of these occurrences in the future. Although we attempt to manage our exposure to such events through the use of underwriting controls and the purchase of third-party reinsurance, catastrophic events are inherently unpredictable and the actual nature of such events when they occur could be more frequent or severe than contemplated in our pricing and risk management expectations. As a result, the occurrence of one or more catastrophic events could have a material adverse effect on our results of operations or financial condition.

Although Florida has not experienced a hurricane during the last six hurricane seasons, some weather analysts believe that we have entered a period of greater hurricane activity. To address this risk, we are exploring alternatives to reduce our exposure to these types of storms. Although these measures may increase operating expenses, management believes that they will assist us in protecting long-term profitability, although there can be no assurances that will be the case.

We have exhausted the reinsurance coverage available for Hurricane Wilma and if any claims exceed this coverage amount, it could adversely impact our business, results of operations and/or financial condition.

As of December 31, 2011 the loss experience (both paid and not yet paid) in connection with Hurricane Wilma which occurred in October 2005 has exhausted the $194.8 million reinsurance coverage available to us. Currently, we hold $2.3 million in open reserves connected with Hurricane Wilma. We have realized $1.5 million in excess of our reinsurance coverage for Hurricane Wilma as of December 31, 2011. If payments to settle the Hurricane Wilma claims exceed our open reserves it could have an adverse impact on our business, results of operations and financial condition.

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

We have a reinsurance structure that is a combination of private reinsurance and the FHCF. Our reinsurance structure is comprised of several reinsurance companies with varying levels of participation providing coverage for loss and LAE at pre-established minimum and maximum amounts. Losses incurred in connection with a catastrophic event below the minimum and above the maximum are the responsibility of Federated National.

The availability and costs associated with the acquisition of reinsurance will vary year to year. These fluctuations, which can be significant, are not subject to our control and may limit our ability to purchase adequate coverage. The recovery of increased reinsurance costs through rate action is not immediate and cannot be presumed, as it is subject to Florida OIR approval.

We face a risk of non-collectibility of reinsurance, which could materially and adversely affect our business, results of operations and/or financial condition.

As is common practice within the insurance industry, we transfer a portion of the risks insured under our policies to other companies through the purchase of reinsurance. This reinsurance is maintained to protect our insurance subsidiary against the severity of losses on individual claims, unusually serious occurrences in which a number of claims produce an aggregate extraordinary loss and catastrophic events. Although reinsurance does not discharge our insurance subsidiary from its primary obligation to pay for losses insured under the policies it issues, reinsurance does make the assuming reinsurer liable to the insurance subsidiary for the reinsured portion of the risk. A credit exposure exists with respect to ceded losses to the extent that any reinsurer is unable or unwilling to meet the obligations assumed under the reinsurance contracts. The collectibility of reinsurance is subject to the solvency of the reinsurers, interpretation of contract language and other factors. A reinsurer's insolvency or inability to make payments under the terms of a reinsurance contract could have a material adverse effect on our results of operations and financial condition.

Our reinsurance structure has significant risks, including the fact that the FHCF may not be able to raise sufficient money to pay their claims or impair their ability to pay their claims in a timely manner. This could result in significant financial, legal and operational challenges to our company. Therefore, in the event of a catastrophic loss, we may become dependent upon the FHCF's ability to pay, which may, in turn, be dependent upon the FHCF's ability to issue bonds in amounts that would be required to meet its reinsurance obligations in the event of such a catastrophic loss.

Our January 2011 Consent Order with the Florida OIR limits our business in certain respects and may prevent us from growing our business.

In January 2011, we entered into a Consent Order with the Florida OIR in connection with our request for approval of the merger of Federated National into American Vehicle. See “Regulation – Consent Order”. Among other things, the Consent Order requires us to reduce the concentration of our homeowners’ policies in the Tri-County Area. This reduction in concentration could materially adversely affect us by limiting our ability to write policies in the most populous region of the State of Florida, which could materially adversely affect our results of operations if we are not able to replace those policies with policies elsewhere in Florida or the other states in which we do business.

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

Our future growth will depend on our ability to expand the types of insurance products we offer and the geographic markets in which we do business, both balanced by the business risks we choose to assume and cede. We believe that our Company is sufficiently capitalized to operate our business as it now exists and as we currently plan to expand it. Our existing sources of funds include possible sales of our investment securities and our earnings from operations and investments. Unexpected catastrophic events in our market areas, such as the hurricanes experienced in Florida, have resulted and may result in greater claims losses than anticipated, which could require us to limit or halt our growth while we redeploy our capital to pay these unanticipated claims.

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

Our future capital requirements depend on many factors, including our ability to write new business successfully and to establish premium rates and reserves at levels sufficient to cover losses. Based on our current operating plan, we believe current capital, together with our anticipated retained earnings, will support our operations without the need to raise additional capital. To the extent that our capital may be insufficient to meet future operating requirements and/or cover losses, we may need to raise additional funds through financings or curtail our growth. Many factors will affect the amount and timing of our capital needs, including our growth and profitability, our claims experience, and the availability of reinsurance, as well as possible acquisition opportunities, market disruptions and other unforeseeable developments.

If we were required to raise additional capital, equity or debt financing may not be available at all or may be available only on terms that are not favorable to us. In the case of equity financings, dilution to our stockholders’ ownership could result, and in any case such securities may have rights, preferences and privileges that are senior to those of existing shareholders. If we cannot obtain adequate capital on favorable terms or at all, our business, financial condition or results of operations could be materially adversely affected.

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

We are subject to extensive regulation in the states in which we conduct business. This regulation is generally designed to protect the interests of policyholders, as opposed to shareholders and other investors, and relates to authorization for lines of business, capital and surplus requirements, investment limitations, underwriting limitations, transactions with affiliates, dividend limitations, changes in control, premium rates and a variety of other financial and non-financial components of an insurance company's business. The NAIC and state insurance regulators are constantly reexamining existing laws and regulations, generally focusing on modifications to holding company regulations, interpretations of existing laws and the development of new laws.

From time to time, some states in which we conduct business have considered or enacted laws that may alter or increase state authority to regulate insurance companies and insurance holding companies. In other situations, states in which we conduct business have considered or enacted laws that impact the competitive environment and marketplace for property and casualty insurance. In addition, in recent years the state insurance regulatory framework has come under increased federal scrutiny. Changes in federal legislation and administrative policies in several areas, including changes in the Gramm-Leach-Bliley Act, financial services regulation and federal taxation, can significantly impact the insurance industry and us.

We cannot predict with certainty the effect any enacted, proposed or future state or federal legislation or NAIC initiatives may have on the conduct of our business. Furthermore, there can be no assurance that the regulatory requirements applicable to our business will not become more stringent in the future or result in materially higher costs than current requirements. Changes in the regulation of our business may reduce our profitability, limit our growth or otherwise adversely affect our operations.

We may experience financial exposure from climate change.

Our financial exposure from climate change is most notably associated with losses in connection with the occurrence of hurricanes striking Florida. We mitigate the risk of financial exposure from climate change by restrictive underwriting criteria, sensitivity to geographic concentrations and reinsurance.

Restrictive underwriting criteria can include, but are not limited to, higher premiums and deductibles and more specifically excluded policy risks such as fences and screened-in enclosures. New technological advances in computer generated geographical mapping afford us an enhanced perspective as to geographic concentrations of policyholders and proximity to flood prone areas. Our amount of maximum reinsurance coverage is 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. Our amount of losses retained (our deductible) in connection with a catastrophic event is determined by market capacity, pricing conditions and surplus preservation.

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

We maintain reserves to cover our estimated ultimate liabilities for loss and LAE. These reserves are estimates based on historical data and statistical projections of what we believe the settlement and administration of claims will cost based on facts and circumstances then known to us. Actual loss and LAE reserves, however, may vary significantly from our estimates.

Factors that affect unpaid losses and LAE include the estimates made on a claim-by-claim basis known as "case reserves" coupled with bulk estimates known as IBNR. Periodic estimates by management of the ultimate costs required to settle all claim files are based on our 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.

Because of the uncertainties that surround estimated loss reserves, we cannot be certain that our reserves will be adequate to cover our actual losses. If our reserves for unpaid losses and LAE are less than actual losses and LAE, we will be required to increase our reserves with a corresponding reduction in our net income in the period in which the deficiency is identified. Future loss experience substantially in excess of our reserves for unpaid losses and LAE could substantially harm our results of operations and financial condition.

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

We operate in a regulatory environment where certain entities and organizations have the authority to require us to participate in assessments. Currently these entities and organizations include, but are not limited to, the Florida Joint Underwriters Association ("JUA"), FIGA, Citizens and the FHCF. The current assessments stem from the catastrophic effects to the property insurance industry in the state of Florida from the hurricanes that occurred during the fourteen months between August 2004 and October 2005.

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Several of the assessments resulted in a charge to current operations. The insurance companies currently pass the assessments on to insurance policies, in the form of a policy surcharge, and reflect the collection of these assessments as fully earned credits to operations in the period collected. The collection of these fees may adversely affect our overall marketing strategy due to the competitive landscape in Florida. Future assessments are likely, although the impact of these assessments on our balance sheet, results of operations or cash flow are undeterminable at this time.

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

As do other insurance companies, we depend on income from our investment portfolio for a substantial portion of our earnings. During the time that normally elapses between the receipt of insurance premiums and any payment of insurance claims, we invest the funds received, together with our other available capital, primarily in debt securities and to a lesser extent in equity securities, in order to generate investment income.

Our investment portfolio contains interest rate sensitive instruments, such as bonds, which may be adversely affected by changes in interest rates. A significant increase in interest rates or decrease in credit worthiness could have a material adverse effect on our financial condition or results of operations. Generally, bond prices decrease as interest rates rise. Changes in interest rates could also have an adverse effect on our investment income and results of operations. For example, if interest rates decline, investment of new premiums received and funds reinvested will earn less than expected.

We may experience a loss due to the concentration of credit risk.

Financial instruments that potentially subject the Company to significant concentration of credit risk consist of cash and cash equivalents held in a mutual fund money market account. The Company had approximately $6.8 million and $14.2 million invested in the MTB Prime Money Market-Inst Fund Number 142, for which the NAIC classification is Class 1, as of December 31, 2011 and 2010, respectively. A money market fund is eligible for listing on the Class 1 list if the fund meets certain characteristics relating to the credit rating, net asset value and other criteria demonstrating the financial condition of the fund.

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

In conjunction with our ongoing reporting obligations as a public company and the requirements of Section 404 of the Sarbanes-Oxley Act, management reported on the effectiveness of our internal control over financial reporting as of December 31, 2011. In order to identify any material weaknesses in our internal control over financial reporting, we engaged in a process to document, evaluate and test our internal controls and procedures, including corrections to existing controls and implement additional controls and procedures that we may deem necessary. As a result of this evaluation and testing process, no material financial reporting deficiencies were noted.

Although we did not have any material weaknesses in our internal controls for our fiscal year ended December 31, 2011, we cannot be certain that there will be none in the future. In future periods, if the process required by Section 404 of the Sarbanes-Oxley Act reveals significant deficiencies or material weaknesses, the correction of any such significant deficiencies or material weaknesses could require additional remedial measures that could be costly and time-consuming. In addition, the discovery of material weaknesses could also require the restatement of prior period operating results. If a material weakness exists as of a future period year-end (including a material weakness identified prior to year-end for which there is an insufficient period of time to evaluate and confirm the effectiveness of the corrections or related new procedures), our management will be unable to report favorably as of such future period

year-end as to the effectiveness of our control over financial reporting and we could lose investor confidence in the accuracy and completeness of our financial reports, which could have an adverse effect on our stock price and potentially subject us to litigation.

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

Various provisions of our policies, such as limitations or exclusions from coverage which have been negotiated to limit our risks, may not be enforceable in the manner we intend. At the present time we employ a variety of exclusions to our policies that limit exposure to known risks, including, but not limited to, exclusions relating to certain named liabilities, types of vehicles and specific artisan activities.

In addition, the policies we issue contain conditions requiring the prompt reporting of claims to us and our right to decline coverage in the event of a violation of that condition. While our insurance product exclusions and limitations reduce the loss exposure to us and help eliminate known exposures to certain risks, it is possible that a court or regulatory authority could nullify or void an exclusion or legislation could be enacted modifying or barring the use of such endorsements and limitations in a way that would adversely affect our loss experience, which could have a material adverse effect on our financial condition or results of operations.

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

As industry practices and legal, judicial, social and other conditions change, unexpected and unintended issues related to claims and coverage may emerge. These issues may adversely affect our business by either extending coverage beyond our underwriting intent or by increasing the number or size of claims. In some instances, these changes may not become apparent until sometime after we have issued insurance contracts that are affected by the changes. As a result, the full extent of liability under our insurance contracts may not be known for many years after a contract is issued.

An example of such emerging change is the influence public adjusters have had on property claim patterns. Public adjusters represented the vast majority of new and reopened claims filed during 2011, 2010 and 2009 where the cause of loss was asserted as hurricane related. Although the legitimacy of the claim may not prevail we are still required to research, review and sometimes mediate these claims. Several legislative actions in the state of Florida, such as limiting the time a claim can be filed subsequent to the cause of loss, have either passed or remain in legislative sub-committees. Each of these actions is designed to enhance the legitimacy of the public adjusters' influence on the claim process.

The Company's operating results in 2011, 2010 and 2009 were also influenced by legislative enactments relating to claims payments. Following the 2004 and 2005 hurricane seasons, the Florida legislature required all insurers issuing replacement cost policies to pay the full replacement cost of damaged properties without deducting depreciation whether or not the insureds repaired or replaced the damaged property. Under prior law, insurers would pay the depreciated amount of the property until insureds commenced repairs or replacement. The new law has led to an increase in disagreements regarding the scope of damage and has resulted in insureds' not repairing damage. Despite our efforts to adjust claims and promptly pay meritorious amounts, our operating results have been affected by a claims environment in Florida that produces opportunities for fraudulent or overstated claims.

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

We must accurately evaluate and pay claims that are made under our policies. Many factors affect our ability to pay claims accurately, including the training and experience of our claims representatives, the culture of our claims organization and the effectiveness of our management, our ability to develop or select and implement appropriate procedures and systems to support our claims functions and other factors. Our failure to pay claims accurately could lead to material litigation, undermine our reputation in the marketplace, impair our image and negatively affect our financial results.

In addition, if we do not train new claims adjusting employees effectively or if we lose a significant number of experienced claims adjusting employees, our claims department's ability to handle an increasing workload as we grow could be adversely affected. In addition to potentially requiring that growth be slowed in the affected markets, we could suffer decreased quality of claims work, which in turn could lower our operating margins.

Our insurance company is subject to minimum capital and surplus requirements, and our failure to meet these requirements could subject us to regulatory action.

Our insurance company is subject to risk-based capital standards and other minimum capital and surplus requirements imposed under applicable state laws, including the laws of their state of domicile, Florida. The risk-based capital standards, based upon the Risk Based Capital Model Act adopted by the NAIC require our insurance company to report their results of risk-based capital calculations to state departments of insurance and the NAIC. These risk-based capital standards provide for different levels of regulatory attention depending upon the ratio of an insurance company's total adjusted capital, as calculated in accordance with NAIC guidelines, to its authorized control level risk-based capital. Authorized control level risk-based capital is the number determined by applying the NAIC's risk-based capital formula, which measures the minimum amount of capital that an insurance company needs to support its overall business operations.

Any failure by our insurance company to meet the applicable risk-based capital or minimum statutory capital requirements imposed by the laws of Florida or other states where we do business could subject it to further examination or corrective action imposed by state regulators, including limitations on our writing of additional business, state supervision or liquidation. As of December 31, 2011, Federated National was in compliance with the NAIC risk-based capital requirements (see "Business-Regulation" for further discussion).

Any changes in existing risk-based capital requirements or minimum statutory capital requirements may require us to increase our statutory capital levels, which we may be unable to do.

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

Historically, the financial performance of the property and casualty insurance industry has tended to fluctuate in cyclical patterns characterized by periods of significant competition in pricing and underwriting terms and conditions, which is known as a "soft" insurance market, followed by periods of lessened competition and increasing premium rates, which is known as a "hard" insurance market. Although an individual insurance company's financial performance is dependent on its own specific business characteristics, the profitability of most property and casualty insurance companies tends to follow this cyclical market pattern, with profitability generally increasing in hard markets and decreasing in soft markets. At present, we are experiencing a hardening market in the property and casualty market in Florida because of regulatory changes. We cannot predict, however, how long these market conditions will persist. We do not compete entirely on price or targeted market share. Our ability to compete is governed by our ability to assess and price an insurance product with an acceptable risk for obtaining profit.

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

The insurance industry is highly regulated. Prior to selling a new insurance product in a state, we must obtain approval from the applicable state insurance regulators. The insurance regulators in states to which we might apply may request additional information, add conditions to the license that we find unacceptable, or deny our application. This would delay or prevent us from operating in that state. If we want to operate in any additional states, we must file similar applications for licenses, which we may not be successful in obtaining.

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

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

The withdrawal of our ratings could limit or prevent us from writing or renewing desirable insurance policies, from competing with insurers who have higher ratings, from obtaining adequate reinsurance, or from borrowing on a line of credit. The withdrawal of our ratings could have a material adverse effect on the Company’s results of operations and financial position because the Company’s insurance products might no longer be acceptable to the secondary marketplace and mortgage lenders. Furthermore, a withdrawal of our ratings could prevent independent agents from selling and servicing our insurance products.

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

We currently market and distribute Federated National's products and services through contractual relationships with a network of approximately 3,000 independent agents, of which approximately 600 actively sell and service our products, and a selected number of general agents. Our independent agents are our primary source for our automobile and property insurance policies. Many of our competitors also rely on independent agents. As a result, we must compete with other insurers for independent agents' business. Our competitors may offer a greater variety of insurance products, lower premiums for insurance coverage, or higher commissions to their agents. If our products, pricing and commissions do not remain competitive, we may find it more difficult to attract business from independent agents to sell our products. A material reduction in the amount of our products that independent agents sell could negatively affect our revenues.

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

Our business is highly dependent upon the successful and uninterrupted functioning of our current information technology and telecommunications systems. We rely on these systems to process new and renewal business, provide customer service, make claims payments and facilitate collections and cancellations, as well as to perform actuarial and other analytical functions necessary for pricing and product development. As a result, the failure of these systems could interrupt our operations and adversely affect our financial results. We utilize a third-party to provide certain information security related services designed to prevent an information security event or detect one timely. In addition, although we have implemented security measures to protect our systems from computer viruses and intrusions by third parties, there can be no assurances that these measures will be effective.

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

Nonstandard automobile insurance is provided to insureds that are unable to obtain preferred or standard insurance coverage because of their payment histories, driving records, age, vehicle types, or prior claims histories. This type of automobile insurance historically has a higher frequency of claims than does preferred or standard automobile insurance policies, although the average dollar amount of the claims is usually smaller under nonstandard insurance policies. As a result, we are exposed to the possibility of increased loss exposure and higher claims experience than would be the case if we offered only standard automobile insurance.

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

Florida's personal injury protection insurance statute limits an insurer's ability to deny benefits for medical treatment that is unrelated to the accident, that is unnecessary, or that is fraudulent. In addition, the statute allows claimants to obtain awards for attorney's fees. Although this statute has been amended several times in recent years, primarily to address concerns over fraud, the Florida legislature has been only marginally successful in implementing effective mechanisms that allow insurers to combat fraud and other abuses. We believe that this statute contributes to a higher frequency of claims under nonstandard automobile insurance policies in Florida, as compared with claims under standard automobile insurance policies in Florida and nonstandard and standard automobile insurance policies in other states. Although we believe that we have successfully offset these higher costs with premium increases, because of competition, we may not be able to do so with as much success in the future.

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

The results of our operations and the financial condition of our insurance company depends on our ability to underwrite and set premium rates accurately for a wide variety of risks. Rate adequacy is necessary to generate sufficient premiums to pay losses, LAE and underwriting expenses and to earn a profit. In order to price our products accurately, we must collect and properly analyze a substantial amount of data; develop, test and apply appropriate rating formulas; closely monitor and timely recognize changes in trends; and project both severity and frequency of losses with reasonable accuracy. Our ability to undertake these efforts successfully, and as a result price our products accurately, is subject to a number of risks and uncertainties, some of which are outside our control, including:

- the availability of sufficient reliable data and our ability to properly analyze available data;

- the uncertainties that inherently characterize estimates and assumptions;
- our selection and application of appropriate rating and pricing techniques;
- changes in legal standards, claim settlement practices, medical care expenses and restoration costs; and
- legislatively imposed consumer initiatives.

Consequently, we could under-price risks, which would negatively affect our profit margins, or we could overprice risks, which could reduce our sales volume and competitiveness. In either event, the profitability of our insurance company could be materially and adversely affected.

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

We currently intend to expand our product offerings by underwriting additional insurance products and programs, and marketing them through our distribution network. Expansion of our product offerings will result in increases in expenses due to additional costs incurred in actuarial rate justifications, software and personnel. Offering additional insurance products may also require regulatory approval, further increasing our costs. There can be no assurance that we will be successful bringing new insurance products to our marketplace.

Increased competition, competitive pressures, industry developments and market conditions could affect the growth of our business and adversely impact our financial results.

We operate in highly competitive markets and face competition from national, regional and residual market insurance companies in the homeowners', commercial residential property, commercial general liability, and automobile markets, many of whom are larger, have greater financial and other resources, and offer more diversified insurance coverage. Our competitors include companies that market their products through agents, as well as companies that 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. Competition could have a material adverse effect on our business, results of operations and financial condition. If we do not meet the prices offered by our competitors, we may lose business in the short term, which could also result in reduced revenues.

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

We depend, and will continue to depend, on the services of our executive management team which includes Michael Braun, our Chief Executive Officer and President of 21st Century Holding Company and Federated National, and Peter Prygelski, our Chief Financial Officer. Our success also will depend in part upon our ability to attract and retain qualified executive officers, experienced underwriting talent and other skilled employees who are knowledgeable about our business. If we were to lose the services of members of our executive management team, our business could be adversely affected. Although we have employment agreements with our executive officers, any unplanned loss of service could substantially harm our business.

Risks Related to an Investment in Our Shares

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

Our articles of incorporation authorize the issuance of preferred stock with designations, rights and preferences determined from time to time by our board of directors. Accordingly, our board of directors is empowered, without shareholder approval, to issue preferred stock with dividends, liquidation, conversion, voting or other rights that could adversely affect the voting power or other rights of the holders of common stock. In addition, the preferred stock could be issued as a method of discouraging a takeover attempt. Although we do not intend to issue any preferred stock at this time, we may do so in the future.

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

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Our articles of incorporation and bylaws contain provisions that may discourage takeover attempts and may result in entrenchment of management.

- Our board of directors is elected in classes, with only two or three of the directors elected each year. As a result, shareholders would not be able to change the membership of the board in its entirety in any one year. Shareholders would also be unable to bring about, through the election of a new board of directors, changes in our officers.

- Our articles of incorporation prohibit shareholders from acting by written consent, meaning that shareholders will be required to conduct a meeting in order to vote on any proposals or take any action.

- Our bylaws require at least 60 days' notice if a shareholder desires to submit a proposal for a shareholder vote or to nominate a person for election to our board of directors.

In addition, Florida has enacted legislation that may deter or frustrate takeovers of Florida corporations, such as our Company.

- The Florida Control Share Act provides that shares acquired in a "control share acquisition" will not have voting rights unless the voting rights are approved by a majority of the corporation's disinterested shareholders. A "control share acquisition" is an acquisition, in whatever form, of voting power in any of the following ranges: (a) at least 20% but less than 33-1/3% of all voting power, (b) at least 33-1/3% but less than a majority of all voting power; or (c) a majority or more of all voting power.

- The Florida Affiliated Transactions Act requires supermajority approval by disinterested shareholders of certain specified transactions between a public company and holders of more than 10% of the outstanding voting shares of the corporation (or their affiliates).

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

We are an insurance holding company whose primary assets are the stock of our subsidiaries. Our operations, and our ability to service future potential debt, are limited by the earnings of our subsidiaries and their payment of their earnings to us in the form of management fees, commissions, dividends, loans, advances or the reimbursement of expenses. These payments can be made only when our subsidiaries have adequate earnings. In addition, dividend payments made to us by our insurance subsidiary is restricted by Florida law governing the insurance industry. Generally, Florida law limits the dividends payable by insurance companies under complicated formulas based on the subsidiary's available capital and earnings.

In the first quarter of 2010 we paid quarterly dividends of $0.06 per share. In response to the capital infusion from American Vehicle during March 2010, the Florida OIR has required that the Company not expend capital on the payment of dividends or the buyback of the Company’s common stock until Federated National experiences two consecutive quarters with an underwriting profit; hence no additional dividends were paid during 2011 or 2010. Additionally, the January 2011 consent order prohibits the Company from paying dividends. Payment of dividends in the future will depend on OIR approval, our earnings and financial position and such other factors, as our Board of Directors deems relevant. Moreover, our ability to continue to pay dividends may be restricted by regulatory limits on the amount of dividends that Federated National is permitted to pay to the parent company.

ITEM 1B UNRESOLVED STAFF COMMENTS

None

ITEM 2 PROPERTIES

Relative to the Company’s commitments stemming from operational matters, on or about March 1, 2006 we sold our interest in the building which housed our operations in Lauderdale Lakes through December 16, 2011, to an unrelated party. As part of this transaction, we agreed to lease the same facilities for a five-year term. We amended the lease agreement and the note receivable on September 1, 2010. As part of the amendment, we discounted the note receivable and have discontinued the interest on the note. In consideration, we paid a reduced lease payment for the remainder of the lease. Our lease for this office space expired in December 2011.

Our executive offices are now located at 14050 N.W. 14th Street, Suite 180, Sunrise, Florida 33323 in an 18,500 square feet office facility. All of our operations are consolidated within this facility. We believe that the facilities are well maintained, in substantial compliance with environmental laws and regulations, and adequately covered by insurance. We also believe that these leased facilities are not unique and could be replaced, if necessary, at the end of

the lease term. Our lease for this office space will expire in May 2017.

ITEM 3 LEGAL PROCEEDINGS

See Item 8 of Part II, “Financial Statements and Supplementary Data – Footnote 9 – Commitments and Contingencies”.

ITEM 4 MINE SAFETY DISCLOSURES

Not applicable.

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PART II

ITEM 5 MARKET FOR REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock is listed for trading on The NASDAQ Global Market under the symbol "TCHC". The following table sets out the high and low closing sale prices as reported on The NASDAQ Global Market. These reported prices reflect inter-dealer prices without adjustments for retail markups, markdowns or commissions.

Quarter Ended	High	Low
March 31, 2011	$ 3.46	$ 3.07
June 30, 2011	$ 3.05	$ 2.58
September 30, 2011	$ 2.80	$ 2.30
December 31, 2011	$ 2.96	$ 2.32
March 31, 2010	$ 4.60	$ 3.96
June 30, 2010	$ 4.10	$ 3.55
September 30, 2010	$ 3.95	$ 3.26
December 31, 2010	$ 3.74	$ 3.14

As of March 5, 2012, there were 26 holders of record of our common stock. We believe that the number of beneficial owners of our common stock is in excess of 3,200.

DIVIDENDS

In the first quarter of 2010 we paid quarterly dividends of $0.06 per share. No further dividends were paid in 2010 or 2011, pursuant to applicable regulatory requirements and our Consent Order with the Florida OIR (see "Regulation – Consent Order").

Payment of dividends in the future will depend on approval of the Florida OIR and our earnings and financial position and such other factors, as our Board of Directors deems relevant. Moreover, our ability to pay dividends may be restricted by regulatory limits on the amount of dividends that Federated National is permitted to pay to the parent company.

SECURITIES AUTHORIZED FOR ISSUANCE UNDER EQUITY COMPENSATION PLANS

The following table summarizes our equity compensation plans as of December 31, 2011. All equity compensation plans were approved by our shareholders. We have not granted any options, warrants or rights to our shareholders outside of these equity compensation plans.

Equity Compensation Plan Information

Plan category	Number of securities to be issued upon exercise of outstanding	Weighted-average exercise price of outstanding options, warrants and	Number of securities remaining available for future issuance

	options, warrants and rights (a)	rights (b)	under equity compensation plans (excluding securities reflected in column (a)) (c)
Equity compensation plans approved by stock holders*	714,450	$ 6.98	180,448

* Includes options from the 1998 Stock Option Plan and the 2002 Stock Option Plan.

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For additional information concerning our capitalization please see Footnote 14 to our Consolidated Financial Statements included under Item 8 of this Annual Report on Form 10-K.

ISSUER REPURCHASES

During 2011 and 2010, the Company did not repurchase any common stock under previously announced stock repurchase plans.

SALES OF UNREGISTERED SECURITIES

None.

ITEM 6 SELECTED FINANCIAL DATA

The following selected consolidated financial data should be read in conjunction with the consolidated financial statements and notes thereto and "Management's Discussion and Analysis of Financial Condition and Results of Operations" appearing elsewhere in this Annual Report on Form 10-K.

	As of the years ended December 31, (Amounts in Thousands except Book Value Per Share)				
	2011	2010	2009	2008	2007
Balance Sheet Data					
Total assets	$179,980	$184,049	$202,889	$197,102	$219,361
Investments	129,467	122,485	114,219	26,065	136,224
Cash and short term investments	15,205	16,206	28,197	124,577	22,524
Finance contracts, consumer loans and pay advances receivable, net	-	-	-	-	420
Total liabilities	121,836	126,118	135,447	120,871	138,104
Unpaid losses and LAE	59,983	66,529	70,611	64,775	59,685
Unearned premiums	47,933	47,136	50,857	40,508	56,394
Total shareholders' equity	58,144	57,931	67,442	76,231	81,257
Book value per share	$7.32	$7.29	$8.48	$9.51	$10.32

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	Years Ended December 31, (Amounts in Thousands except EPS and Dividends)				
	2011	2010	2009	2008	2007
Operations Data:					
Revenue:					
Gross premiums written	$98,269	$96,410	$104,379	$88,248	$133,591
Gross premiums ceded	(46,293)	(52,963)	(56,217)	(34,553)	(44,550)
Net premiums written	51,976	43,447	48,162	53,695	89,041
(Decrease) Increase in prepaid reinsurance premiums	(2,656)	(2,108)	10,163	(4,451)	(11,251)
(Increase) Decrease in unearned premiums	(797)	3,721	(10,349)	15,886	21,435
Net change in prepaid reinsurance premiums and unearned premiums	(3,453)	1,613	(186)	11,435	10,184
Net premiums earned	48,523	45,060	47,976	65,130	99,224
Commission income	994	1,388	1,362	1,612	7,214
Finance revenue	518	395	294	350	545
Managing general agent fees	1,583	1,609	1,620	1,745	2,035
Net investment income	4,079	3,726	3,397	6,461	8,038
Net realized investment gains (losses)	2,725	6,777	1,117	(10,593)	(145)
Regulatory assessments recovered	109	857	2,333	2,104	1,655
Other income	1,632	792	755	655	642
Total revenue	60,163	60,604	58,854	67,464	119,208
Expenses:					
Losses and LAE	30,896	40,088	43,706	41,869	47,619
Operating and underwriting expenses	9,916	10,835	9,681	7,209	12,758
Salaries and wages	8,004	8,611	7,930	7,428	6,732
Interest expense	-	-	-	-	173
Policy acquisition costs - amortization	12,347	13,025	13,747	14,760	19,420
Total expenses	61,163	72,559	75,064	71,266	86,702
(Loss) income before provision for income tax (benefit) expense	(1,000)	(11,955)	(16,210)	(3,802)	32,506
Provision for income tax (benefit) expense	(570)	(3,959)	(5,921)	(1,324)	11,226
Net (loss) income	$(430)	$(7,996)	$(10,289)	$(2,478)	$21,280
Earnings per share data					
Net (loss) income per share - basic	$(0.05)	$(1.01)	$(1.29)	$(0.31)	$2.69
Net (loss) income per share - dilluted	$(0.05)	$(1.01)	$(1.29)	$(0.31)	$2.65

Dividends paid per share	$-	$0.06	$0.36	$0.72	$0.72

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21st Century Holding Company
Management's Discussion and Analysis of Financial Condition and Results of Operations

ITEM 7 MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

OVERVIEW

We are an insurance holding company that controls substantially all steps in the insurance underwriting, distribution and claims processes through our subsidiaries and our contractual relationships with our independent agents and general agents.

We are authorized to underwrite, and/or place through our wholly owned subsidiaries, homeowners' multi-peril ("homeowners"), commercial general liability, personal and commercial automobile, personal umbrella, fire, allied lines, workers' compensation and commercial inland marine insurance in Florida and various other states. We market and distribute our own and third-party insurers' products and our other services through a network of independent agents. We also utilize a select number of general agents for the same purpose.

• Our primary insurance subsidiary is Federated National Insurance Company ("Federated National"). Federated National is licensed as an admitted carrier in Florida. An admitted carrier is an insurance company that has received a license from the state department of insurance giving the company the authority to write specific lines of insurance in that state. Through contractual relationships with a network of approximately 3,000 independent agents, of which approximately 600 actively sell and service our products, Federated National is authorized to underwrite homeowners', fire, allied lines and personal and commercial automobile insurance in Florida. Federated National is also licensed as an admitted carrier in Alabama, Louisiana, Georgia and Texas, and underwrites commercial general liability insurance in those states. Federated National operated as a non-admitted carrier in Arkansas, California, Kentucky, Maryland, Missouri, Nevada, Oklahoma, South Carolina, Tennessee and Virginia, and could underwrite commercial general liability insurance in all of these states. A non-admitted carrier is allowed to do business in that state and is strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud. Sometimes, non-admitted carriers are referred to as "excess and surplus" lines carriers. Non-admitted carriers are subject to considerably less regulation with respect to policy rates and forms. Non-admitted carriers are not required to financially contribute to and benefit from the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due their policyholders.

In January 2011, we merged Federated National and our other wholly owned insurance subsidiary, American Vehicle Insurance Company ("American Vehicle"), with Federated National continuing the operations of both entities. In connection with this merger, the Company, Federated National and American Vehicle entered into a Consent Order with the Florida Office of Insurance Regulation ("Florida OIR") pursuant to which we agreed to certain restrictions on our a business operations. See "Regulation – Consent Order".

• We internally process claims made by our insureds through our wholly owned claims adjusting company, Superior Adjusting, Inc. ("Superior"). Until June 2011, we offered premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium Finance, Inc. ("Federated Premium").

• Assurance Managing General Agents, Inc. ("Assurance MGA"), a wholly owned subsidiary of the Company, acts as Federated National's exclusive managing general agent in Florida and is also licensed as a managing general agent in the States of Alabama, Georgia, Illinois, Louisiana, North Carolina, Mississippi, Missouri, New York, Nevada, South Carolina, Texas and Virginia. Assurance MGA has contracted with several unaffiliated insurance companies to sell commercial general liability, workers compensation, personal umbrella and inland marine insurance

through Assurance MGA's existing network of agents.

Assurance MGA earns commissions and fees for providing policy administration, marketing, accounting and analytical services, and for participating in the negotiation of reinsurance contracts. Assurance MGA earns a $25 per policy fee, and traditionally a 6% commission fee from its affiliates Federated National and American Vehicle. During the fourth quarter of 2010, Assurance MGA, pursuant to the Consent Order as discussed in "Regulation – Consent Order" reduced its fee, to earn amounts varying between 2% and 4%, which we anticipate will return to 6% at an unknown future date with approval from the Florida OIR. A formal agreement reflecting this fee modification was executed during January 2011.

Although we are authorized to underwrite the various lines described above, our business is primarily underwriting homeowners' policies. During 2011, 81.8%, 10.3%, 4.6% and 3.3% of the premiums we underwrote were for homeowners', commercial general liability, federal flood, and personal automobile insurance, respectively. During 2010, 79.7%, 12.3%, 4.1% and 3.9% of the premiums we underwrote were for homeowners', commercial general liability, federal flood, and personal automobile insurance, respectively.

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

During the years ended December 31, 2011, 2010 or 2009, we did not experience any weather-related catastrophic events such as the hurricanes that occurred in Florida during 2005 and 2004. We are not able to predict how hurricanes or other insurable events will affect our future results of operations and liquidity. Loss and loss adjustment expenses ("LAE") are affected by a number of factors, many of which are partially or entirely beyond our control, including the following.

- the nature and severity of the loss;
- weather-related patterns;
- the availability, cost and terms of reinsurance;
- underlying settlement costs, including medical and legal costs;
- legal and political factors such as legislative initiatives and public opinion;
- macroeconomic issues.

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 us. When our estimated liabilities for unpaid losses and LAE are less than the actuarially determined amounts, we increase the expense in the current period. Conversely, when our estimated liabilities for unpaid losses and LAE are greater than the actuarially determined amounts, we decrease the expense in the current period.

Our goal in our reinsurance strategy is to equalize the liquidity requirements imposed by most severe insurable events and by all other insurable events we manage in the normal course of business. Please see "Reinsurance Agreements" under "Item 1. Business" for a more detailed description of our reinsurance agreements and strategy.

CRITICAL ACCOUNTING POLICIES

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

The most significant accounting estimates inherent in the preparation of our financial statements include estimates associated with management's evaluation of the determination of (i) liability for unpaid losses and LAE, (ii) the amount and recoverability of amortization of Deferred Policy Acquisition Costs ("DPAC"), and (iii) estimates for our reserves with respect to finance contracts, premiums receivable and deferred income taxes. Various assumptions and other factors underlie the determination of these significant estimates, which are described in greater detail in Footnote 2 in this Form 10-K.

Except as described below, we believe that in 2011 there were no significant changes in those critical accounting policies and estimates. Senior management has reviewed the development and selection of our critical accounting policies and estimates and their disclosure in this Form 10-K with the Audit Committee of our Board of Directors.

The process of determining significant estimates is fact-specific and takes into account factors such as historical experience, current and expected economic conditions, and in the case of unpaid losses and LAE, an actuarial valuation. Management regularly reevaluates these significant factors and makes adjustments where facts and circumstances dictate. In selecting the best estimate, we utilize various actuarial methodologies. Each of these

methodologies is designed to forecast the number of claims we will be called upon to pay and the amounts we will pay on average to settle those claims. In arriving at our best estimate, our actuaries consider the likely predictive value of the various loss development methodologies employed in light of underwriting practices, premium rate changes and claim settlement practices that may have occurred, and weight the credibility of each methodology. Our actuarial methodologies take into account various factors, including, but not limited to, paid losses, liability estimates for reported losses, paid allocated LAE, salvage and other recoveries received, reported claim counts, open claim counts and counts for claims closed with and without payment for loss.

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

FASB issued guidance addresses accounting and reporting for (a) investments in equity securities that have readily determinable fair values and (b) all investments in debt securities. The guidance requires that these securities be classified into one of three categories: Held-to-maturity, Trading, or Available-for-sale securities.

Investments classified as held-to-maturity include debt securities wherein the Company's intent and ability are to hold the investment until maturity. The accounting treatment for held-to-maturity investments is to carry them at amortized cost without consideration to unrealized gains or losses. Investments classified as trading securities include debt and equity securities bought and held primarily for the sale in the near term. The accounting treatment for trading securities is to carry them at fair value with unrealized holding gains and losses included in current period operations. Investments classified as available-for-sale include debt and equity securities that are not classified as held-to-maturity or as trading security investments. The accounting treatment for available-for-sale securities is to carry them at fair value with unrealized holding gains and losses excluded from earnings and reported as a separate component of shareholders' equity, namely "Other Comprehensive Income".

Overview of Management's Loss Reserving Process

The Company's loss reserves can generally be categorized into two distinct groups. One group is short-tail classes of business consisting principally of property risks in connection with homes and automobiles. The other group is long-tail casualty classes of business which include primarily commercial general liability and to a much lesser extent, homeowner and automobile liability. For operations writing short-tail coverages our loss reserves were generally geared toward determining an expected loss ratio for current business rather than maintaining a reserve for the outstanding exposure. Estimations of ultimate net loss reserves for long-tail casualty classes of business is a more complex process and depends on a number of factors including class and volume of business involved. Experience in the more recent accident years of long-tail casualty classes of business shows limited statistical credibility in reported net losses because a relatively low proportion of net losses would be reported claims and expenses and even smaller percentage would be net losses paid. Therefore, incurred but not yet reported ("IBNR") would constitute a relatively high proportion of net losses.

Additionally, the different methodologies are utilized the same, regardless of the line of business. However, the final selection of ultimate loss and LAE is certain to vary by both line of business and by accident period maturity. There is no prescribed combination of line of business, accident year maturity, and methodologies; consistency in results of the different methodologies and reasonableness of the result are the primary factors that drive the final selection of ultimate loss and LAE.

Methods Used to Estimate Loss and LAE Reserves

The methods we use for our short-tail business do not differ from the methods we use for our long-tail business. The Incurred and Paid Development Methods intrinsically recognize the unique development characteristics contained within the historical experience of each material short-tail and long-tail line of business. The Incurred and Paid Cape Cod Methods reflect similar historical development unique to each material short-tail and long-tail line of business.

We apply the following general methods in projecting loss and LAE reserves:

- Paid and Incurred Loss Development Method
- Paid and Incurred Bornhuetter-Ferguson Incurred Method

- Frequency / Severity Method

Description of Ultimate Loss Estimation Methods

The estimated Ultimate Loss and Defense and Cost Containment Expense (“DCCE”) is based on an analysis by line of business, coverage and by accident quarter performed using data as of December 31, 2011. The analysis relies primarily on four actuarial methods: Incurred Loss and DCCE Development Method, Paid Loss and DCCE Development Method, Bornhuetter-Ferguson Incurred Method, and Bornhuetter-Ferguson Paid Method. Each method relies on company experience, and, where relevant, the analysis includes comparisons to industry experience. The following is a description of each of these methods:

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Incurred Loss and DCCE Development Method – This reserving method is based on the assumption that the historical incurred loss and DCCE development pattern as reflected by the Company is appropriate for estimating the future loss & DCCE development. Incurred paid plus case amounts separated by accident quarter of occurrence and at quarterly evaluations are used in this analysis. Case reserves do not have to be adequately stated for this method to be effective; they only need to have a fairly consistent level of adequacy at all stages of maturity. Historical "age-to-age" loss development factors were calculated to measure the relative development of an accident quarter from one maturity point to the next. Loss and DCCE development factors ("LDF") are selected based on a review of the historical relationships between incurred loss & DCCE at successive valuations and based on industry patterns. The LDFs are multiplied together to derive cumulative LDF's that, when multiplied by actual incurred loss and DCCE, produce estimates of ultimate loss and DCCE.

Paid Loss & DCCE Development Method – This method is similar to the Incurred Loss & DCCE Development Method only paid loss & DCCE and paid patterns are substituted for the incurred loss & DCCE and incurred patterns.

Bornhuetter-Ferguson Incurred Method – This reserving method combines estimated initial expected unreported loss & DCCE with the actual loss & DCCE to yield the ultimate loss & DCCE estimate. Expected unreported loss & DCCE are equal to expected total loss & DCCE times the expected unreported percentage of loss & DCCE for each policy year. The incurred loss & DCCE emergence pattern used to determine the unreported percentages in our projections is based on the selected LDF's from the Incurred Loss & DCCE Development Method described above. The estimate of initial expected total loss & DCCE is based on the historical loss ratio for more mature accident years. While this approach reduces the independence of the Bornhuetter-Ferguson Method from the loss & DCCE development methods for older policy years, it is used primarily for estimating ultimate loss & DCCE for more recent, less mature, policy years.

Bornhuetter-Ferguson Paid Method – This method is similar to the Bornhuetter-Ferguson Incurred Method only paid loss & DCCE and paid patterns are substituted for the incurred loss & DCCE and incurred patterns.

We select an estimate of ultimate loss & DCCE for each accident quarter after considering the results of each projection method for the quarter and the relative maturity of the quarter (the time elapsed between the start of the quarter and December 31, 2011). Reserves for unpaid losses & DCCE for each quarter are the differences between these ultimate estimates and the amount already paid. The reserves for each quarter and each coverage are summed, and the result is the overall estimate of unpaid losses & DCCE liability for the company.

We also produce an estimate of unpaid Adjusting and Other Expense ("A&O"), as a reserve is required under Statutory Accounting Principles ("SAP") even if this expense has been pre-paid or with an unconsolidated affiliate. Although we do not prepay for A&O, the majority of the A&O incurred is with an affiliated company and eliminated under the accounting principles for consolidation. The unpaid A&O is added to unpaid losses & DCCE, resulting in total unpaid losses and LAE.

The validity of the results from using a loss development approach can be affected by many conditions, such as internal claim department processing changes, a shift between single and multiple claim payments, legal changes, or variations in a company's mix of business from year to year. Also, since the percentage of losses paid for immature years is often low, development factors can be volatile. A small variation in the number of claims paid can have a leveraging effect that could lead to significant changes in estimated ultimate values. Accordingly, our reserves are estimates because there are uncertainties inherent in the determination of ultimate losses. Court decisions, regulatory changes and economic conditions can affect the ultimate cost of claims that occurred in the past as well as create

uncertainties regarding future loss cost trends. We compute our estimated ultimate liability using the most appropriate principles and procedures applicable to the lines of business written. However, because the establishment of loss reserves is an inherently uncertain process, we cannot be certain that ultimate losses will not exceed the established loss reserves and have a material adverse effect on our results of operations and financial condition.

Frequency / Severity Method – This method separately estimates the two components of ultimate losses (the frequency, or number of claims and the severity, or cost per claim) and then combines the resulting estimates in a multiplicative fashion to estimate ultimate losses. The approach is valuable because sometimes there is more inherent stability in the frequency and severity data when viewed separately than in the total losses.

We developed reported claim counts to ultimate levels using the development approach. The mechanics of this approach are the same as we described previously for paid and incurred losses. The validity of the results of this method depends on the stability of claim reporting and settlement rates. Then we developed accident year incurred severities (incurred losses divided by reported claim counts) to ultimate levels using the development approach.

We trended these severities to accident year 2011 levels. Trend rates were selected based on a review of historical severities. Selected severity was chosen based on judgment considering the developed severities and the trended severities, considering industry benchmarks for each segment. The loss & ALAE, claim count and severity triangles are evaluated as of 12 months, 24 months, 36 months etc. We selected loss development factors based on the loss development history, to the extent credible, and supplemented with industry data where appropriate.

A key assumption underlying the estimation of the reserve for loss and LAE is that past experience serves as the most reliable estimator of future events. This assumption may materially affect the estimates when the insurance market, the regulatory environment, the legal environment, the economic environment, the book of business, the claims handling department, or other factors (known or unknown) have varied over time during the experience period and / or will vary (expectedly or unexpectedly) in the future. Changes in estimates, or differences between estimates and amounts ultimately paid, are reflected in the operating results of the period during which such adjustments are made. Therefore, the ultimate liability for unpaid losses and LAE will likely differ from the amount recorded at December 31, 2011.

The following describes the extent of our procedures for determining the reserve for loss and LAE on both an annual and interim reporting basis:

Annually - Our policy is to select a single point estimate that best reflects our in-house actuarial determination for unpaid losses and LAE. Our independent actuarial firm, examining the exact same data set, will independently select a point estimate which determines a high point and low point range. Both processes rely on objective and subjective determinations. If our point estimate falls within the range determined from the point estimate of our actuary, then the Company's policy has been that no adjustments by management would be required. In consideration thereof, the company does not have a policy for adjusting the liability for unpaid losses and LAE to an amount that is different than an amount set forth within the range determined by our independent actuary, although the reserve level ultimately determined by us may not be the mid-point of our independent actuary's range. Further, there can be no assurances that our actual losses will be within our actuary's range. Our independent actuary's report expressly states that the report is based on assumptions developed from its own analysis and based on information provided by management and that notwithstanding its analysis, there is a significant risk of material adverse deviation from its range.

Interim – During 2011 our interim approach was very similar to the annual process noted above.

A number of other actuarial assumptions are generally made in the review of reserves for each class of business.

- For each class of business, expected ultimate loss ratios for each accident year are estimated based on loss reserve development patterns. The expected loss ratio generally reflects the projected loss ratio from prior accident years, adjusted for the loss trend and the effect of rate changes and other quantifiable factors on the loss ratio.

In practice there are factors that change over time; however, many (such as inflation) are intrinsically reflected in the historical development patterns, and others typically do not materially affect the estimate of the reserve for unpaid losses and LAE. Therefore, no specific adjustments have been incorporated for such contingencies projecting future development of losses and LAE. There are no key assumptions as of December 31, 2011 premised on future emergence inconsistent with historical loss reserve development patterns.

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The table below distinguishes total loss reserves between IBNR, as discussed above, and case estimates for specific claims as established by routine claims management.

Reserves for unpaid loss and LAE net of reinsurance recoverable as of December 31, 2011	Case Loss Reserves	Case LAE Reserves	Total Case Reserves	IBNR Reserves (Including LAE)	Reinsurance Recoverable on Unpaid Loss and Loss Expenses	Net Reserves
	(Dollars in Thousands)					
Homeowners'	$6,719	$1,571	$8,290	$12,328	$ 480	$20,138
Commercial General Liability	2,369	1,606	3,975	28,089	(190)	32,254
Automobile	3,428	113	3,541	3,511	1,798	5,254
Fire	8	2	10	238	-	248
Inland Marine	-	-	-	1	-	1
Total	$12,524	$3,292	$15,816	$44,167	$ 2,088	$57,895

Reserves for unpaid loss and LAE net of reinsurance recoverable as of December 31, 2010	Case Loss Reserves	Case LAE Reserves	Total Case Reserves	IBNR Reserves (Including LAE)	Reinsurance Recoverable on Unpaid Loss and Loss Expenses	Net Reserves
	(Dollars in Thousands)					
Homeowners'	$4,829	$975	$5,804	$16,695	$ 5,508	$16,991
Commercial General Liability	5,620	2,610	8,230	27,817	-	36,047
Automobile	3,353	112	3,465	4,366	1,302	6,529
Fire	-	3	3	148	-	151
Inland Marine	-	-	-	1	-	1
Total	$13,802	$3,700	$17,502	$49,027	$ 6,810	$59,719

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Our reported results, financial position and liquidity would be affected by likely changes in key assumptions that determine our net loss reserves. The table below illustrates the change to equity that would occur as a result of a change in loss and LAE reserves, net of reinsurance.

	Years Ended December 31, 2011		2010	
Change in loss and LAE reserves, net of reinsurance	Adjusted loss and LAE reserves, net of reinsurance	Percentage change in equity (1)	Adjusted loss and LAE reserves, net of reinsurance	Percentage change in equity (1)
	(Dollars in Thousands)			
-10.0 %	52,106	-7.5 %	53,747	-20.8 %
-7.5 %	53,553	-5.6 %	55,240	-15.6 %
-5.0 %	55,000	-3.7 %	56,733	-10.4 %
-2.5 %	56,448	-1.9 %	58,226	-5.2 %
Base	57,895	-	59,719	-
2.5 %	59,343	1.9 %	61,212	5.2 %
5.0 %	60,790	3.7 %	62,705	10.4 %
7.5 %	62,237	5.6 %	64,198	15.6 %
10.0 %	63,685	7.5 %	65,691	20.8 %

(1) Net of tax

For the year ended December 31, 2011, our actuarial firm determined range of statutory loss and LAE reserves on a net basis range from a low of $51.5 million to a high of $65.2 million, with a best estimate of $55.4 million. The Company's net loss and LAE reserves are carried on a statutory basis at $55.6 million, and on a GAAP consolidated basis at $60.0 million which when netted with our $2.1 million reinsurance recoverable totals $57.9 million. The Company's point estimate for its reserves as of December 31, 2011 is 0.3% above our actuary's best estimate, which reflects management's current analysis of the status and expected timing of our anticipated claims, our analysis of expected weather patterns in the regions in which we sell policies, our re-focus of our business growth efforts to areas outside of South Florida, and other factors.

We are required to review the contractual terms of all our reinsurance purchases to ensure compliance with FASB issued guidance. The guidance establishes the conditions required for a contract with a reinsurer to be accounted for as reinsurance and prescribes accounting and reporting standards for those contracts. Contracts that do not result in the reasonable possibility that the reinsurer may realize a significant loss from the insurance risk assumed generally do not meet the conditions for reinsurance accounting and must be accounted for as deposits. The guidance also requires us to disclose the nature, purpose and effect of reinsurance transactions, including the premium amounts associated with reinsurance assumed and ceded. It also requires disclosure of concentrations of credit risk associated with reinsurance receivables and prepaid reinsurance premiums.

Please see Footnote 2 of the Notes to Consolidated Financial Statements for additional discussions regarding critical accounting policies.

RECENT ACCOUNTING PRONOUNCEMENTS

See Note 2(n), “Summary of Significant Accounting Policies – Recent Accounting Pronouncements” in the Notes to the Condensed Consolidated Financial Statements for a discussion of recent accounting pronouncements and their effect, if any, on the Company.

ANALYSIS OF FINANCIAL CONDITION
As of December 31, 2011 Compared with December 31, 2010

Total Investments

Total investments increased $7.0 million, or 5.7%, to $129.5 million as of December 31, 2011, compared with $122.5 million as of December 31, 2010.

We account for our investment securities consistent with FASB-issued guidance that requires our securities to be classified into one of three categories: (i) held-to-maturity, (ii) trading securities or (iii) available-for-sale.

Investments classified as held-to-maturity include debt securities where the Company's intent and ability are to hold the investment until maturity and are carried at amortized cost without consideration to unrealized gains or losses. Investments classified as trading securities include debt and equity securities bought and held primarily for sale in the near term and are carried at fair value with unrealized holding gains and losses included in current period operations. Investments classified as available-for-sale include debt and equity securities that are not classified as held-to-maturity or as trading security investments and are carried at fair value with unrealized holding gains and losses excluded from earnings and reported as a separate component of shareholders' equity, namely "Other Comprehensive Income."

The debt and equity securities that are available for sale and carried at fair value represent 94% of total investments as of December 31, 2011, compared with 95% as of December 31, 2010.

We did not hold any trading investment securities during 2011.

As of December 31, 2011 and 2010, our investments consisted primarily of corporate bonds held in various industries, municipal bonds and United States government bonds. As of December 31, 2011, 61% of our debt portfolio was in diverse industries and 39% is in United States government bonds. As of December 31, 2011, approximately 83% of our equity holdings were in equities related to diverse industries and 17% were in mutual funds. As of December 31, 2010, 72% of our debt portfolio was in diverse industries and 28% was in United States government bonds. As of December 31, 2010, approximately 77% of our equity holdings were in equities related to diverse industries and 23% were in mutual funds.

Below is a summary of net unrealized gains and losses at December 31, 2011 and December 31, 2010 by category.

	Unrealized Gains and (Losses)	
	December 31, 2011	December 31, 2010
	(Dollars in Thousands)	
Debt securities:		
United States government obligations and authorities	$659	$(192)
Obligations of states and political subdivisions	138	43
Corporate	1,543	268
International	5	24
	2,345	143

Equity securities:		
Common stocks	(939)	692
Total debt and equity securities	$1,406	$835

The net unrealized gain of $1.4 million is inclusive of $2.4 million of unrealized losses. The $2.4 million of unrealized losses is inclusive of $2.0 million unrealized losses from equity securities and $0.4 million unrealized losses from debt securities.

The $2.0 million of unrealized losses from equity securities is from common stocks and mutual funds held in diverse industries as of December 31, 2011. The Company evaluated the near-term prospects in relation to the severity and duration of the impairment. Based on this evaluation and the Company's ability and intent to hold these investments for a reasonable period of time sufficient for a forecasted recovery of fair value, the Company does not consider these investments to be other-than-temporarily impaired at December 31, 2011.

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The $0.4 million of unrealized losses from debt securities is related to both corporate and US government bonds. The Company does not expect to settle at prices less than the amortized cost basis. The Company does not consider these investments to be other-than-temporarily impaired at December 31, 2011 because we neither currently intend to sell these investments nor consider it likely that we will be required to sell these investments before recovery of the amortized cost basis; additionally, at least 74% of these bonds had at least an “A” rating.

FASB has also issued guidance regarding when an investment is considered impaired, whether that impairment is other-than temporary, and the measurement of an impairment loss. Management periodically reviews the individual investments that comprise our portfolio in order to determine whether a decline in fair value below our cost either is other-than temporarily or permanently impaired. Factors used in such consideration include the extent and length of time over which the market value has been less than cost, the financial condition and near-term prospects of the issuer and our ability and intent to keep the investment for a period sufficient to allow for an anticipated recovery in market value. In reaching a conclusion that a security is either other-than-temporarily or permanently impaired, we also consider such factors as the timeliness and completeness of expected dividends, principal and interest payments, ratings from nationally recognized statistical rating organizations such as Standard and Poor’s and Moody’s Investors Service, Inc. (“Moody’s”), as well as information released via the general media channels. During 2011, in connection with the process, we have charged to operations $0.8 million of investment losses. During 2010, in connection with this process, we have not charged any net realized investment loss to operations.

As of December 31, 2011 and December 31, 2010, all of our securities are in good standing and not impaired, except as noted above.

The Company records the unrealized losses, net of estimated income taxes, that are associated with that part of our portfolio classified as available-for-sale through the shareholders' equity account titled “Other Comprehensive Income”.

The following table summarizes, by type, our investments as of December 31, 2011 and 2010.

	December 31, 2011		December 31, 2010	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
Debt securities, at market:				
United States government obligations and authorities	$37,217	28.75 %	$28,196	23.02 %
Obligations of states and political subdivisions	2,303	1.77 %	2,963	2.42 %
Corporate	63,268	48.87 %	65,808	53.73 %
International	1,523	1.18 %	1,383	1.13 %
	104,311	80.57 %	98,350	80.30 %
Debt securities, at amortized cost:				
Corporate	962	0.74 %	818	0.67 %
United States government obligations and authorities	6,166	4.76 %	5,380	4.39 %
	7,128	5.50 %	6,198	5.06 %
Total debt securities	111,439	86.07 %	104,548	85.36 %
Equity securities, at market:	18,028	13.93 %	17,937	14.64 %
Total investments	$129,467	100.00 %	$122,485	100.00 %

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Debt securities are carried on the balance sheet at market. At December 31, 2011 and 2010, debt securities had the following quality ratings by S&P and for securities not assigned a rating by S&P, Moody's or Fitch ratings were used.

	December 31, 2011		December 31, 2010	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
AAA	$ 48,686	43.69 %	$ 43,533	41.64 %
AA	6,712	6.02 %	8,995	8.60 %
A	31,960	28.68 %	39,079	37.38 %
BBB	22,193	19.92 %	11,125	10.64 %
Not rated	1,888	1.69 %	1,816	1.74 %
	$ 111,439	100.00 %	$ 104,548	100.00 %

The following table summarizes, by maturity, the debt securities as of December 31, 2011 and 2010.

	December 31, 2011		December 31, 2010	
	Carrying Amount	Percent of Total	Carrying Amount	Percent of Total
	(Dollars in Thousands)			
Matures In:				
One year or less	$ 8,328	7.47 %	$ 13,267	12.69 %
One year to five years	48,176	43.24 %	50,149	47.96 %
Five years to 10 years	37,380	33.54 %	29,979	28.68 %
More than 10 years	17,555	15.75 %	11,153	10.67 %
Total debt securities	$ 111,439	100.00 %	$ 104,548	100.00 %

At December 31, 2011, the weighted average maturity of the debt portfolio was approximately 7.5 years.

As of December 31, 2011 and December 31, 2010, we have classified $7.1 million and $6.2 million, respectively, of our bond portfolio as held-to-maturity. We only classify bonds as held-to-maturity to support securitization of credit requirements.

During 2011, we did not re-classify any of our bond portfolio between available-for-sale and held-to-maturity.

During 2010, we re-classified $3.1 million of amortized cost to held-to-maturity from available-for-sale to fund trust agreements.

As of December 31, 2011 and December 31, 2010, Federated National maintained fully funded trust agreements that totaled $4.6 million in favor of two of its reinsurers.

During April 2006, American Vehicle finalized a $15.0 million irrevocable letter of credit in conjunction with the 100% Quota Share Reinsurance Agreement with Republic Underwriters Insurance Company ("Republic") which was terminated in April 2007. During 2010, the letter of credit in favor of Republic was replaced by a fully funded trust agreement. As of December 31, 2011 and 2010 respectively, the amount held in trust was $1.0 million.

Cash and Short-Term Investments

Cash and short-term investments, which include cash, certificates of deposits, and money market accounts, decreased $1.0 million, or 6.2%, to $15.2 million as of December 31, 2011, compared with $16.2 million as of December 31, 2010. The decrease in cash and short-term investments resulted from portfolio reallocation based on improving risk profiles; wherein we decided to increase our exposure to corporate bonds. We evaluate our asset class allocation on an ongoing basis continually adjust based on economic and business risk.

Prepaid Reinsurance Premiums

Prepaid reinsurance premiums decreased $2.1 million, or 19.9%, to $8.3 million as of December 31, 2011, compared with $10.4 million as of December 31, 2010. The change is due to $0.6 million of ceded premiums, net of payments to reinsurers, reduced by $2.7 million amortization of prepaid reinsurance premiums associated with our reinsurance programs. We believe concentrations of credit risk associated with our prepaid reinsurance premiums are not significant.

Premiums Receivable, Net of Allowance for Credit Losses

Premiums receivable, net of allowance for credit losses, remained unchanged at $5.6 million as of December 31, 2011, compared with $5.6 million as of December 31, 2010.

Our homeowners' insurance premiums receivable increased $0.2 million, or 6.6%, to $3.7 million as of December 31, 2011, compared with $3.5 million as of December 31, 2010.

Our commercial general liability insurance premiums receivable decreased $0.2 million, or 15.2%, to $1.2 million as of December 31, 2011, compared with $1.4 million as of December 31, 2010.

Premiums receivable in connection with our automobile line of business remained unchanged at $0.8 million as of December 31, 2011, compared with $0.8 million as of December 31, 2010.

Our allowance for credit losses remained unchanged at $0.1 million as of December 31, 2011, compared with $0.1 million as of December 31, 2010.

	Years Ended December 31, 2011	2010
	(Dollars in Thousands)	
Allowance for credit losses at beginning of year	$ 68	$ 24
Additions charged to bad debt expense	115	135
Write-downs charged against the allowance	(110)	(91)
Allowance for credit losses at end of year	$ 73	$ 68

Reinsurance Recoverable, Net

Reinsurance recoverable, net, decreased $5.9 million, or 74.0%, to $2.1 million as of December 31, 2011, compared with $8.0 million as of December 31, 2010. The change is due to the payment patterns by our reinsurers, as influenced by the diminishing catastrophe related claims. All amounts are current and deemed collectable. We believe concentrations of credit risk associated with our reinsurance recoverables, net, are not significant.

Deferred Policy Acquisition Costs

DPAC decreased $0.2 million, or 2.0%, to $7.7 million as of December 31, 2011, compared with $7.9 million as of December 31, 2010. The change is due to the deferral of the actual policy acquisition costs, including commissions, payroll and premium taxes, less commissions earned on reinsurance ceded and policy fees earned. An analysis of

deferred acquisition costs follows.

	Years Ended December 31,	
	2011	2010
	(Dollars in Thousands)	
Balance, beginning of year	$ 7,879	$ 8,267
Acquisition costs deferred	12,186	12,637
Amortization expense during year	(12,347)	(13,025)
Balance, end of year	$ 7,718	$ 7,879

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Deferred Income Taxes, Net

Deferred income taxes, net, increased $0.7 million, or 8.8%, to $8.6 million as of December 31, 2011, compared with $7.9 million as of December 31, 2010. Deferred income taxes, net, is comprised of approximately $12.1 million and $11.2 million of deferred tax assets, net of approximately $3.5 million and $3.3 million of deferred tax liabilities as of December 31, 2011 as of December 31, 2010. The change in the net deferred tax asset is primarily due to the increase in the deferred tax assets related to discounted unearned premiums, discount on advanced premiums and net operating losses carry forward.

	Years Ended December 31,	
	2011	2010
Deferred tax assets:		
Unpaid losses and loss adjustment expenses	$2,385	$2,243
Unearned premiums	1,950	1,663
Discount on advance premiums	195	-
Allowance for credit losses	34	-
Allowance for impairments	317	-
Regulatory assessments	-	(69)
Unearned agent commissions (SNSIC)	-	8
Depreciation & amortization	317	393
Reserve for claims settlements	809	809
NOL Carryforward	5,696	5,702
Deferred gain on sale and leaseback	-	100
Stock option expense per ASC 718	410	379
Total deferred tax assets	12,113	11,228
Deferred tax liabilities:		
Deferred acquisition costs, net	(2,905)	(2,965)
Allowance for credit losses	-	(44)
Discount on advance premiums	-	11
Regulatory assessments	(67)	-
Unrealized Gain on investment securities	(529)	(314)
Total deferred tax liabilities	(3,501)	(3,312)
Net deferred tax asset	$8,612	$7,916

Income Taxes Receivable

Income taxes receivable decreased $2.4 million, or 100.0%, to nothing as of December 31, 2011, compared with $2.4 million as of December 31, 2010. The change is due to the receipt of our prior year refund, net of our loss as discussed within "Results of Operations- Year Ended December 31, 2011 Compared with Year Ended December 31, 2010".

The Company's consolidated federal and state income tax returns for 2005-2010 are open for review by the Internal Revenue Service ("IRS") and various state taxing authorities. The federal income tax returns for 2003 and 2002 have been examined by the IRS. The IRS concluded its examination for 2003 and 2002 and there were no material changes in the tax liability for those years. The 2005 and 2006 income tax returns and net operating loss carry-back from tax

year 2009 have been reviewed by the Joint Committee on Taxation. The Joint Committee on Taxation completed its consideration in September 2011 and took no exception to the conclusions reached by the IRS regarding the net operating loss carry-back from tax year 2009.

Other Assets

Other assets decreased $0.2 million, or 9.4%, to $2.1 million as of December 31, 2011, compared with $2.3 million as of December 31, 2010. Major components of other assets are shown in the following table; the accrued interest income receivable is primarily investment related.

	As of December 31,	
	2011	2010
	(Dollars in Thousands)	
Accrued interest income receivable	$1,130	$1,089
Notes receivable	-	365
Deposits	185	133
Prepaid expenses	432	376
Other	347	347
Total	$2,094	$2,310

Unpaid Losses and LAE

Unpaid losses and LAE decreased $6.5 million, or 9.8%, to $60.0 million as of December 31, 2011, compared with $66.5 million as of December 31, 2010. The composition of unpaid losses and LAE by product line is as follows.

	December 31, 2011			December 31, 2010		
	Case	Bulk	Total	Case	Bulk	Total
	(Dollars in Thousands)			(Dollars in Thousands)		
Homeowners'	$8,795	$10,652	$19,447	$5,825	$16,847	$22,672
Commercial General Liability	4,225	27,717	31,942	8,230	27,819	36,049
Automobile	3,533	5,061	8,594	3,447	4,361	7,808
Total	$16,553	$43,430	$59,983	$17,502	$49,027	$66,529

Please see “Liability for Unpaid Losses and LAE” under “Item 1. Business” for a discussion of the factors that affect unpaid losses and LAE.

Unearned Premium

Unearned premiums increased $0.8 million, or 1.7%, to $47.9 million as of December 31, 2011, compared with $47.1 million as of December 31, 2010. The change was due to a $1.5 million increase in unearned homeowners’ insurance premiums, a $0.3 million increase in unearned flood insurance premiums, a $0.6 million decrease in unearned commercial general liability premiums, and a $0.4 million decrease in unearned automobile insurance premiums. Generally, as is in this case, a increase in unearned premium directly relates to a increase in written premium on a rolling twelve-month basis. Competition could negatively affect our unearned premium.

Premium Deposits and Customer Credit Balances

Premium deposits and customer credit balances increased $0.4 million, or 18.6%, to $2.8 million as of December 31, 2011, compared with $2.4 million as of December 31, 2010. Premium deposits are monies received on policies not yet in-force as of December 31, 2011.

Bank Overdraft

Bank overdraft increased $0.5 million, or 6.7%, to $7.9 million as of December 31, 2011, compared with $7.4 million as of December 31, 2010. The bank overdraft relates primarily to losses and LAE disbursements paid but not presented for payment by the policyholder or vendor. The change relates to the timing of presentation of claims checks to the issuing bank.

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Accounts Payable and Accrued Expenses

Accounts payable and accrued expenses increased $0.9 million, or 44.4%, to $3.1 million as of December 31, 2011, compared with $2.2 million as of December 31, 2010. The change from prior year includes increases of $0.2 million for premium taxes payable and $0.1 million for homeowners’ commission payable, as well as the impact of the timing of payments with our trade vendors.

Results of Operations
Year Ended December 31, 2011 Compared with Year Ended December 31, 2010

Effective January 26, 2011, Federated National merged with and into American Vehicle, and the resulting entity changed its name to “Federated National Insurance Company”.

Gross Premiums Written

Gross premiums written increased $1.9 million, or 1.9%, to $98.3 million for 2011, compared with $96.4 million for 2010. The following table denotes gross premiums written by major product line. This increase reflected primarily an increase in the sale of homeowners’ policies.

	Years Ended December 31,			
	2011		2010	
	(Dollars in Thousands)			
	Amount	Percentage	Amount	Percentage
Homeowners'	$80,402	81.82 %	$76,844	79.70 %
Commercial General Liability	10,125	10.30 %	11,894	12.34 %
Federal Flood	4,468	4.55 %	3,951	4.10 %
Automobile	3,274	3.33 %	3,721	3.86 %
Gross written premiums	$98,269	100.00 %	$96,410	100.00 %

The increase in the sale of homeowners’ policies by $3.6 million, or 4.6%, to $80.4 million in 2011, compared with $76.8 million in 2010, is gross of reinsurance costs and net of Florida’s mandated homeowners’ wind mitigation discounts. We offer premium discounts for wind mitigation efforts by policyholders, as required by Florida law. As of December 31, 2011, 63.5% of our in-force homeowners’ policyholders were receiving wind mitigation credits totaling approximately $31.5 million (a 28.6% reduction of in-force premium), while 60.1% of our in-force homeowners’ policyholders were receiving wind mitigation credits totaling approximately $27.3 million, (a 26.0 % reduction of in-force premium), as of December 31, 2010.

During 2011 and 2010, the change to the cumulative wind mitigation credits afforded our policyholders totaled $4.2 million and ($0.3) million, respectively.

These premium discounts have had a significant effect on both written and earned premium. Wind mitigation credits are 28.6% of the pre-credit premium, or $31.5 million, as of December 31, 2011, as compared with 26.0% of the pre-credit premium, or $27.3 million, as of December 31, 2010.

Our in-force homeowners' policies increased by approximately 700, or approximately 2.0%, to approximately 43,800 as of December 31, 2011, as compared with approximately 43,100 as of December 31, 2010.

We received approval from the Florida OIR in 2009 and 2010 for a premium rate increases for our voluntary homeowners' program within the State of Florida. These premium rate increases averaged approximately 19% in 2009 and 20.2% in 2010 and were implemented for policies with effective dates as soon as permitted following approval. In addition, in 2010 we received approval from the Florida OIR for a premium rate increase of approximately 15% for homeowners policies assumed from Citizens Property Insurance Corporation ("Citizens") in Florida beginning July 2010. In February 2012, we received approval from the Florida OIR of a 14.1% rate increase. That rate increase, together with our 2011 rate increases for our voluntary property book of homeowners' business, averaging 20.2% statewide, and our assumed property book of homeowners' business, averaging 13.9% statewide, are expected to gain momentum and accrete throughout 2012.

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Our earnings can also be impacted by our ratings, such as the rating of Federated National by Demotech, Inc. ("Demotech"). Federated National's rating as of December 31, 2011 was "A" ("Exceptional"). For more information regarding our rating and the impact of a change or withdrawal of our rating, please see "Business-Regulation-Industry Rating Services."

The Company's sale of commercial general liability policies decreased by $1.8 million to $10.1 million for 2011, compared with $11.9 million for 2010. The primary factor for this decrease has been improvements to our underwriting standards and our decision to restrict underwriting authority within specific commercial general liability classes and geographic areas.

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

	Years Ended December 31,			
	2011		2010	
	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)			
State				
Alabama	$ 57	0.56 %	$ 46	0.39 %
Arkansas	-	0.00 %	1	0.01 %
California	8	0.08 %	34	0.29 %
Florida	8,606	84.99 %	9,972	83.85 %
Georgia	-	0.00 %	68	0.57 %
Kentucky	-	0.00 %	-	0.00 %
Louisiana	916	9.05 %	1,094	9.19 %
Maryland	-	0.00 %	9	0.07 %
Oklahoma	2	0.02 %	-	0.00 %
South Carolina	2	0.02 %	1	0.01 %
Texas	534	5.28 %	665	5.59 %
Virginia	-	0.00 %	4	0.03 %
Total	$ 10,125	100.00 %	$ 11,894	100.00 %

We are required to report write-your-own flood premiums on a direct and 100% ceded basis.

The Company's sale of auto insurance policies decreased to $3.3 million for 2011, compared with $3.7 million 2010. The Company's sale of auto insurance included only renewal policies in 2011 , and new and renewal policies in 2010.

Gross Premiums Ceded

Gross premiums ceded decreased to $46.3 million for 2011, compared with $53.0 million for 2010. Gross premiums ceded relating to our homeowners', write-your-own flood and automobile programs totaled $40.3 million, $4.5 million and $1.5 million for 2011. Gross premiums ceded relating to our homeowners', commercial general liability, write-your-own flood and automobile programs totaled $46.9 million, $0.2 million, $4.0 million and $1.9 million for 2010.

The decrease to gross premiums ceded relating to our homeowners' program is primarily due to the reduced cost of reinsurance purchased from the Florida Hurricane Catastrophe Fund ("FHCF"). The ceded relating to our automobile program is associated with our arrangement to write nonstandard private passenger automobile insurance through a reputable managing general agent familiar with the Georgia market. A quota share treaty cedes 100% of the risk and fully collateralizes for unearned premium and unpaid loss and LAE.

Decrease in Prepaid Reinsurance Premiums

The decrease in prepaid reinsurance premiums was $2.7 million in 2011, compared with a $2.1 million decrease in 2010. The increased charge to written premium is associated with the timing of our reinsurance payments measured against the term of the underlying reinsurance policies.

(Increase) Decrease in Unearned Premiums

The increase in unearned premiums was $0.8 million for 2011, compared with a $3.7 million decrease for 2010. The 2011 charge to written premium was due to a $1.5 million increase in unearned homeowners' insurance premiums, a $0.3 million increase in unearned flood premiums, a $0.4 million decrease in unearned automobile premiums and a $0.6 million decrease in unearned commercial general liability premiums during 2011. These changes are a result of differences in written premium volume during this period as compared with the same period last year. See "Gross Premiums Written" above.

Net Premiums Earned

Net premiums earned increased $3.4 million, or 7.7%, to $48.5 million for 2011, compared with $45.1 million for 2010. The following table denotes net premiums earned by product line.

	Years Ended December 31,			
	2011		2010	
	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)			
Homeowners'	$35,785	73.75 %	$30,040	66.67 %
Commercial General Liability	10,632	21.91 %	13,302	29.52 %
Automobile	2,106	4.34 %	1,718	3.81 %
Net premiums earned	$48,523	100.00 %	$45,060	100.00 %

The $5.7 million increase in homeowners' net premiums earned is due to a $3.6 million increase in gross written premium as discussed, a $6.5 million decrease in gross premiums ceded and a $4.4 million decrease in the net change to prepaid reinsurance premiums and unearned premium.

The $2.7 million decrease in commercial general liability net premiums earned is a result of a $1.8 million decrease in gross written premium, reflecting the impact our decision to restrict underwriting authority within specific commercial general liability classes and geographic areas. The change is also a result of a $0.2 million decrease in gross premiums ceded and a $1.1 million decrease in the net change to unearned premium.

The $0.4 million increase in automobile net premiums earned is a result of a $0.4 million decrease in gross written premium as discussed, a $0.3 million decrease in gross premiums ceded and a $0.5 million increase in the net change to prepaid reinsurance premiums and unearned premium.

Commission Income

Commission income decreased $0.4 million, or 28.4%, to $1.0 million for 2011, compared with $1.4 million for 2010. The primary sources of our commission income are our managing general agent services, write-your-own flood premiums and our independent insurance agency, Insure-Link, Inc. ("Insure-Link").

Net Investment Income

Net investment income increased $0.4 million, or 9.5%, to $4.1 million for 2011, compared with $3.7 million for 2010. Our investment yield, net and gross of investment expenses, excluding equities and including cash, were 2.9% and 3.1%, respectively, for 2011. Our investment yield, net and gross of investment expenses, excluding equities and including cash, were 2.5% and 2.7%, respectively, for 2010.

Our investment yield, net and gross of investment expenses measured against debt securities, excluding equities and cash, were 3.1% and 3.4%, respectively, for 2011. The primary reason for our lower investment yield in 2011 was the Company harvested gains that were a result of the Federal Reserve's activity in the bond market, which pushed up bond prices and lowered yields. Hence the proceeds from recognizing the gains were reinvested at yields that were lower than what was sold. Our investment yield, net and gross of investment expenses measured against debt securities, excluding equities and cash, were 3.4% and 3.7%, respectively, for 2010.

See also "Analysis of Financial Condition As of December 31, 2011 Compared with December 31, 2010 – Investments" for a further discussion on our investment portfolio.

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Net Realized Investment Gains

Net realized investment gains were $2.7 million for 2011, compared with net realized investment gains of $6.8 million for 2010. Specifically, net realized losses for equity securities were $0.3 million for 2011, compared with $1.7 million net realized gains for 2010. For debt securities, net realized gains were nearly $3.0 million for 2011, compared with net realized gains of $4.0 million for 2010. During 2011, the Company, because of the actions taken by the Federal Reserve to maintain a low interest rate environment, realized significant gains in the fixed income portfolio. During 2010, the Company had an overweight in corporate bonds that performed well and sold these bonds to lock in gains and bolster the surplus of our insurance companies.

FASB has issued guidance regarding when an investment is considered impaired, whether that impairment is other-than temporary, and the measurement of an impairment loss. Management periodically reviews the individual investments that comprise our portfolio in order to determine whether a decline in fair value below our cost either is other-than temporarily or permanently impaired. During 2011, pursuant to guidelines prescribed in FASB issued guidance, we have charged to operations, realized investment losses of $0.8 million. The charges relate to common stock held in diverse industries; during 2010, we did not mark any investments to market value pursuant to guidelines prescribed in FASB issued guidance. In reaching a conclusion that a security is either other than temporarily or permanently impaired we consider such factors as the timeliness and completeness of expected dividends, principal and interest payments, ratings from nationally recognized statistical rating organizations such as Standard and Poor's and Moody's, as well as information released via the general media channels.

The table below depicts the net realized investment gains by investment category during 2011 and 2010.

	Years Ended December 31,	
	2011	2010
	(Dollars in Thousands)	
Realized gains:		
Debt securities	$ 3,569	$ 4,484
Equity securities	1,240	4,228
Total realized gains	4,809	8,712
Realized losses:		
Debt securities	(595)	(209)
Equity securities	(1,489)	(1,726)
Total realized losses	(2,084)	(1,935)
Net realized gains on investments	$ 2,725	$ 6,777

Other Income

Other income increased $0.8 million, or 100.0%, to $1.6 million for 2011, compared with $0.8 million for 2010. The major components of other income for 2011 include $1.1 million from the reconciliation of outstanding checks in connection with our accounting for unclaimed property and $0.5 million in partial recognition of our gain on the sale of our Lauderdale Lakes property. The major components of other income for 2010 included approximately $0.5 million in partial recognition of our gain on the sale of our Lauderdale Lakes property and $0.3 million in recognition of our gain on the sale of a vacant retail property.

Losses and LAE

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

Losses and LAE decreased by $9.2 million, or 22.9%, to $30.9 million for 2011, compared with $40.1 million for 2010. The overall change includes a $7.0 million decrease in our homeowners' program due to favorable experience based in part on enhanced underwriting and claim processing techniques. The overall change also includes a $2.8 million decrease in our commercial general liability program and a $0.6 million increase in connection with our automobile program.

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The composition of unpaid losses and LAE by product line is as follows.

	December 31, 2011			December 31, 2010		
	Case	Bulk	Total	Case	Bulk	Total
	(Dollars in Thousands)			(Dollars in Thousands)		
Homeowners'	$8,795	$10,652	$19,447	$5,825	$16,847	$22,672
Commercial General Liability	4,225	27,717	31,942	8,230	27,819	36,049
Automobile	3,533	5,061	8,594	3,447	4,361	7,808
Total	$16,553	$43,430	$59,983	$17,502	$49,027	$66,529

Please see "Liability for Unpaid Losses and LAE" under "Item 1 Business" for a discussion of the factors that affect unpaid losses and LAE.

Management revises its estimates based on the results of its analysis. This process assumes that 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. Because of our process, reserves were decreased by approximately $6.5 million during 2011. This overall change includes a $3.2 million decrease in reserves for our homeowners' program, a $4.1 million decrease in reserves for our commercial general liability program and a $0.8 million increase in reserves for our automobile program. The decreases are due to favorable experience based in part on enhanced underwriting and claim processing techniques.

Our loss ratio is computed as losses and LAE divided by net premiums earned. A lower loss ratio generally results in higher operating income. Our loss ratio for 2011 was 63.7% compared with 89.0% for the same period in 2010. The favorable decrease to our loss ratio is due to the $9.2 million decrease in losses and LAE measured against the $3.5 million increase in net premium earned during 2011 as compared with the same period in 2010.

The table below reflects the loss ratios by product line.

	Years Ended December 31,			
	2011		2010	
Homeowners'	57.79	%	92.06	%
Commercial General Liability	60.11	%	69.39	%
Automobile	181.63	%	186.30	%
All lines	63.67	%	88.96	%

Operating and Underwriting Expenses

Operating and underwriting expenses decreased $0.9 million, or 8.5%, to $9.9 million for 2011, compared with $10.8 million for 2010. The decreases include $0.4 million in surveys and underwriting reports, $0.3 million in actuarial fees and $0.2 million in insurance expense.

Salaries and Wages

Salaries and wages decreased $0.6 million, or 7.1%, to $8.0 million for 2011, compared with $8.6 million for 2010. The charge to operations for stock-based compensation, in accordance with FASB guidance, was approximately $0.2 million during 2011, compared with approximately $0.4 million for 2010.

Policy Acquisition Costs - Amortization

Policy acquisition costs - amortization, decreased $0.7 million, or 5.2%, to $12.3 million for 2011, compared with $13.0 million for 2010.

Policy acquisition costs - amortization, consists of the actual policy acquisition costs, including commissions, payroll and premium taxes, less commissions earned on reinsurance ceded and policy fees earned.

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Provision for Income Tax Benefit

The provision for income tax benefit was $0.6 million for 2011, compared with a $4.0 million for 2010. The effective rate for income taxes was 57.0% for 2011, compared with 33.1% for 2010. The 57.0% effective rate reflects the true-up of the 2010 tax return permanent differences.

Net Loss

As a result of the foregoing, the Company's net loss for 2011was $0.4 million, compared with $8.0 million for 2010.

Results of Operations
Year Ended December 31, 2010 Compared with Year Ended December 31, 2009

Effective January 26, 2011, Federated National merged with and into American Vehicle, and the resulting entity changed its name to "Federated National Insurance Company".

Gross Premiums Written

Gross premiums written decreased $8.0 million, or 7.6%, to $96.4 million for 2010, compared with $104.4 million for 2009. The following table denotes gross premiums written by major product line. This decrease reflected primarily a decrease in the sale of homeowners' and commercial general liability policies.

	Years Ended December 31,			
	2010		2009	
	(Dollars in Thousands)			
	Amount	Percentage	Amount	Percentage
Homeowners'	$76,844	79.70 %	$84,705	81.15 %
Commercial General Liability	11,894	12.34 %	15,279	14.64 %
Federal Flood	3,951	4.10 %	3,559	3.41 %
Automobile	3,721	3.86 %	836	0.80 %
Gross written premiums	$96,410	100.00 %	$104,379	100.00 %

The decrease in the sale of homeowners' policies by $7.9 million, or 9.3%, to $76.8 million in 2010, compared with $84.7 million in 2009, is gross of reinsurance costs and net of Florida's mandated homeowners' wind mitigation discounts. We offer premium discounts for wind mitigation efforts by policyholders, as required by Florida law. As of December 31, 2010, 60.1% of our in-force homeowners' policyholders were receiving wind mitigation credits totaling approximately $27.3 million (a 26.0% reduction of in-force premium), while 56.8% of our in-force homeowners' policyholders were receiving wind mitigation credits totaling approximately $27.6 million, (a 24.2 % reduction of in-force premium), as of December 31, 2009.

During 2010 and 2009, the change to the cumulative wind mitigation credits afforded our policyholders totaled ($0.3) million and $9.8 million, respectively.

These premium discounts have had a significant effect on both written and earned premium. Wind mitigation credits are 26.0% of the pre-credit premium, or $27.3 million, as of December 31, 2010, as compared with 24.2% of the

pre-credit premium, or $27.6 million, as of December 31, 2009.

As a result of our expanded underwriting criteria, our in-force homeowners' policies decreased by approximately 9,500, or approximately 18.0%, to approximately 43,100 as of December 31, 2010, as compared with approximately 52,600 as of December 31, 2009.

We received approval from the Florida OIR in 2009 and 2010 for a premium rate increases for our voluntary homeowners' program within the State of Florida. These premium rate increases averaged approximately 19% in 2009 and 20.2% in 2010 and were implemented for policies with effective dates as soon as permitted following approval.

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The Company's sale of commercial general liability policies decreased by $3.4 million to $11.9 million in 2010, compared with $15.3 million in 2009. The primary factor for this decrease has been the slowdown in the economy, which had a dramatic impact on the artisan contractor portfolio written by American Vehicle. An additional factor is our decision to restrict underwriting authority within specific commercial general liability classes and geographic areas.

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

	Years Ended December 31,			
	2010		2009	
	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)			
State				
Alabama	$46	0.39 %	$76	0.50 %
Arkansas	1	0.01 %	4	0.03 %
California	34	0.29 %	49	0.32 %
Florida	9,972	83.85 %	12,341	80.77 %
Georgia	68	0.57 %	291	1.91 %
Kentucky	-	0.00 %	1	0.00 %
Louisiana	1,094	9.19 %	1,736	11.36 %
Maryland	9	0.07 %	-	0.00 %
South Carolina	1	0.01 %	2	0.01 %
Texas	665	5.59 %	778	5.09 %
Virginia	4	0.03 %	1	0.01 %
Total	$11,894	100.00 %	$15,279	100.00 %

We are required to report write-your-own flood premiums on a direct and 100% ceded basis.

The Company's sale of auto insurance policies increased to $3.7 million in 2010, compared with $0.8 million in 2009. The Company's sale of auto insurance included new and renewal policies in 2010, but was limited to renewal policies in 2009.

Gross Premiums Ceded

Gross premiums ceded decreased to $53.0 million in 2010, compared with $56.2 million in 2009, due to our decreased cost of reinsurance. Gross premiums ceded under our catastrophe reinsurance program totaled $46.9 million, gross premiums ceded to the write-your-own flood program totaled $4.0 million, gross premiums ceded relating to our commercial automobile program totaled $1.9 million and gross premiums ceded relating to our commercial general liability program totaled $0.2 million in 2010.

(Decrease) Increase in Prepaid Reinsurance Premiums

The decrease in prepaid reinsurance premiums was $2.1 million in 2010, compared with a $10.2 million increase in 2009. The increased charge to written premium is associated with the timing of our reinsurance payments measured against the term of the underlying reinsurance policies.

Decrease (Increase) in Unearned Premiums

The decrease in unearned premiums was $3.7 million in 2010, compared with a $10.3 million increase in 2009. The change was due to a $3.1 million decrease in unearned homeowners' insurance premiums, a $1.6 million decrease in unearned commercial general liability premiums, a $0.8 million increase in unearned automobile premiums, net of a $0.2 million increase in unearned flood premiums in 2010. These changes are a result of differences in written premium volume during this period as compared with the same period last year. See "Gross Premiums Written" above.

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Net Premiums Earned

Net premiums earned decreased $2.9 million, or 6.1%, to $45.1 million for in 2010, compared with $48.0 million in 2009. The following table denotes net premiums earned by product line.

	Years Ended December 31,			
	2010		2009	
	Amount	Percentage	Amount	Percentage
	(Dollars in Thousands)			
Homeowners'	$30,040	66.67 %	$28,474	59.35 %
Commercial General Liability	13,302	29.52 %	19,076	39.76 %
Automobile	1,718	3.81 %	426	0.89 %
Net premiums earned	$45,060	100.00 %	$47,976	100.00 %

The change in homeowners' net premiums earned is due to an $8.0 million decrease in gross written premium as discussed, a $5.6 million decrease in gross premiums ceded and a $3.8 million increase in the net change to prepaid reinsurance premiums and unearned premium.

The change in commercial general liability net premiums earned is a result of a $3.4 million decrease in gross written premium, reflecting the impact of the economic slowdown on the artisan contractor portfolio written by American Vehicle and our decision to restrict underwriting authority within specific commercial general liability classes and geographic areas. The change is also a result of a $0.1 million increase in gross premiums ceded and a $2.3 million decrease in the net change to unearned premium.

The change in automobile net premiums earned is a result of a $2.9 million increase in gross written premium as discussed, a $1.9 million increase in gross premiums ceded and a $0.3 million decrease in the change to unearned premium.

Commission Income

Commission income remained unchanged at $1.4 million in 2010, compared with $1.4 million in 2009. The primary sources of our commission income are our managing general agent services, write-your-own flood premiums and our independent insurance agency, Insure-Link.

Net Investment Income

Net investment income increased $0.3 million, or 9.7%, to $3.7 million in 2010, compared with $3.4 million in 2009. Our investment yield, net and gross of investment expenses, excluding equities and including cash, were 2.5% and 2.7%, respectively, in 2010. Our investment yield, net and gross of investment expenses, excluding equities and including cash, were 2.2% and 2.3%, respectively, in 2009.

Our investment yield, net and gross of investment expenses measured against debt securities, excluding equities and cash, were 3.4% and 3.7%, respectively, in 2010. Our investment yield, net and gross of investment expenses measured against debt securities, excluding equities and cash, were 3.5% and 3.7%, respectively, in 2009.

Net Realized Investment Gains

Net realized investment gains were $6.8 million in 2010, compared with $1.1 million in 2009. Specifically, net realized gains for equity marketable securities were $2.5 million in 2010 compared with $1.5 million in 2009; and for bonds, net realized gains were $4.3 million in 2010, compared with net realized loss of $0.4 million in 2009. Realized investment gains recognized were higher in 2010 than in 2009 because of the Company's investment in marketable securities in diverse industries and an overweight in corporate bonds. These securities performed well in 2010 and were sold to lock in gains and bolster surplus.

During 2010 and 2009, we did not mark any equity investments to market value pursuant to guidelines prescribed in FASB issued guidance. In reaching a conclusion that a security is either other than temporarily or permanently impaired we consider such factors as the timeliness and completeness of expected dividends, principal and interest payments, ratings from nationally recognized statistical rating organizations such as Standard and Poor's and Moody's, as well as information released via the general media channels.

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

The table below depicts the net realized investment gains by investment category in 2010 and 2009.

	Years Ended December 31, 2010	2009
	(Dollars in Thousands)	
Realized gains:		
Debt securities	$ 4,484	$ 485
Equity securities	4,228	2,159
Total realized gains	8,712	2,644
Realized losses:		
Debt securities	(209)	(825)
Equity securities	(1,726)	(702)
Total realized losses	(1,935)	(1,527)
Net realized gains on investments	$ 6,777	$ 1,117

Other Income

Other income remained unchanged at $0.8 million in 2010, compared with $0.8 million in 2009. The major component of other income in 2010 and 2009 included approximately $0.5 million in partial recognition of our gain on the sale of our Lauderdale Lakes property.

Losses and LAE

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

Losses and LAE decreased by $3.6 million, or 8.3%, to $40.1 million in 2010, compared with $43.7 million in 2009. The overall change includes a $1.5 million increase in our homeowners' program and a $6.3 million decrease in our commercial general liability program; these decreases are due to favorable experience in these markets based in part on enhanced underwriting and claim processing techniques. The overall increase also includes a $1.2 million increase in connection with our re-launched automobile program which has experienced adverse development in its initial phase.

The composition of unpaid losses and LAE by product line is as follows.

	December 31, 2010			December 31, 2009		
	Case	Bulk	Total	Case	Bulk	Total
	(Dollars in Thousands)			(Dollars in Thousands)		
Homeowners'	$ 5,825	$ 16,847	$ 22,672	$ 8,705	$ 19,298	$ 28,003
Commercial General Liability	8,230	27,819	36,049	7,885	29,346	37,231
Automobile	3,447	4,361	7,808	2,612	2,765	5,377

Total	$17,502	$49,027	$66,529	$19,202	$51,409	$70,611

Please see “Liability for Unpaid Losses and LAE” under “Item 1. Business” for a discussion of the factors that affect unpaid losses and LAE.

Based on our review as discussed above, reserves were decreased by approximately $4.1 million in 2010. This overall change includes a $5.3 million decrease in our homeowners’ program and a $1.2 million decrease in our commercial general liability program; these decreases are due to favorable experience in these markets based in part on enhanced underwriting and claim processing techniques. The overall decrease also includes a $2.4 million increase in connection with our re-launched automobile program which has experienced adverse development in its initial phase.

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Our loss ratio, which is computed as losses and LAE divided by net premiums earned, in 2010 was 89.0% compared with 91.1% for the same period in 2009.

The table below reflects the loss ratios by product line.

	Years Ended December 31,			
	2010		2009	
Homeowners'	92.06	%	89.62	%
Commercial General Liability	69.39	%	81.30	%
Automobile	186.30	%	629.37	%
All lines	88.96	%	91.10	%

For further discussion, see Footnote 6 to the Consolidated Financial Statements included under Part II, Item 8, of this Report.

Operating and Underwriting Expenses

Operating and underwriting expenses increased $1.1 million, or 11.9%, to $10.8 million in 2010, compared with $9.7 million in 2009. The change is primarily due to a $0.4 million increase in actuarial fees, a $0.2 million increase in consulting fees, a $0.2 million increase in licenses and fees, a less than $0.2 million increase in surveys and underwriting reports, and immaterial increases in other expenses.

Salaries and Wages

Salaries and wages increased $0.7 million, or 8.6%, to $8.6 million in 2010, compared with $7.9 million in 2009. The increase is due to staffing for additional lines of business.

The charge to operations for stock-based compensation, in accordance with FASB issued guidance, remained unchanged at approximately $0.4 million in 2010 compared with approximately $0.4 million in 2009.

Policy Acquisition Costs - Amortization

Policy acquisition costs - amortization, decreased $0.7 million, or 5.2%, to $13.0 million in 2010, compared with $13.7 million in 2009.

Policy acquisition costs - amortization, consists of the actual policy acquisition costs, including commissions, payroll and premium taxes, less commissions earned on reinsurance ceded and policy fees earned.

Provision for Income Tax Benefit

The provision for income tax benefit was $4.0 million in 2010, compared with $5.9 million in 2009. The effective rate for income taxes was 33.1% in 2010 and 36.5% in 2009.

Net Loss

As a result of the foregoing, the Company's net loss in 2010 was $8.0 million compared with $10.3 million in 2009.

CONTRACTUAL OBLIGATIONS

A summary of long-term contractual obligations as of December 31, 2011 follows. The amounts represent estimates of gross undiscounted amounts payable over time.

	(Dollars in Thousands)					
Contractual Obligations	Total	2012	2013	2014	2015	Thereafter
Unpaid Losses and LAE	$59,983	$35,606	$14,342	$6,598	$2,303	$1,134
Operating leases	1,197	130	229	236	243	359
Total	$61,180	$35,736	$14,571	$6,834	$2,546	$1,493

LIQUIDITY AND CAPITAL RESOURCES

In 2011, our primary sources of capital included proceeds from the sale of investment securities, decreased reinsurance recoverable, net, decreased income taxes recoverable, decreased prepaid reinsurance premiums, amortization of investment premium discount, net, increased accounts payable and accrued expenses, increased unearned premiums and increased bank overdraft. Also contributing to our liquidity was increased premium deposits and customer credit balances, non-cash compensation, depreciation and amortization, decreased policy acquisition costs, net of amortization and increased income taxes payable. Because we are a holding company, we are largely dependent upon fees and commissions from our subsidiaries for cash flow.

In 2011, net cash provided by operating activities was $4.2 million. In 2010 and 2009, net cash used by operating activities was $6.5 million and $11.6 million, respectively.

In 2011, operations generated $15.1 million of gross cash flow, due to a $6.0 million decrease in reinsurance recoverable, a $2.4 million decrease in income taxes recoverable, a $2.1 million decrease in prepaid reinsurance premiums, $1.3 million of amortization of investment discount, net, a $1.0 million increase in accounts payable and accrued expenses, a $0.8 million increase in unearned premiums, a $0.5 million increase in bank overdraft, a $0.4 million increase in premium deposits and customer credit balances, $0.3 million of non-cash compensation, $0.2 million of depreciation and amortization and a $0.1 million decrease in policy acquisition costs, net of amortization.

In 2011, operations used $10.9 million of gross cash flow primarily due to a $6.5 million decrease in unpaid losses and LAE, $2.7 million of net realized investment gains, a $0.9 million increase in deferred income tax expense, a $0.3 million increase in various other assets and a less than $0.1 million decrease in the provision for uncollectible premiums receivable, all in conjunction with a net loss of $0.4 million.

In 2011, 2010 and 2009, net cash used by investing activities was $5.2 million, $5.1 million and $82.7 million. Our available for sale investment portfolio is highly liquid as it consists entirely of readily marketable securities. In 2011, investing activities generated $108.3 million and used $113.5 million.

In 2011, net cash provided by financing activities was less than $0.1 million. In 2010 and 2009, net cash used by financing activities was $0.4 million and $2.0 million, respectively. In 2011, the source of cash in connection with financing activities was a tax benefit related to non-cash compensation.

We offer direct billing in connection with our homeowners’, commercial general liability and automobile programs. Direct billing is an agreement in which the insurance company accepts from the insured, as a receivable, a promise to pay the premium, as opposed to requiring the full amount of the policy at policy inception, either directly from the insured or from a premium finance company. The advantage of direct billing a policyholder by the insurance company is that we are not reliant on a credit facility, but remain able to charge and collect interest from the policyholder.

We believe that our current capital resources will be sufficient to meet currently anticipated working capital requirements. There can be no assurances, however, that such will be the case. We continue to evaluate our liquidity and the possibility that we may require additional working capital.

Federated National’s statutory capital surplus as of December 31, 2011 was approximately $39.3 million and its statutory net income in 2011 was $0.8 million.

Federated National's and American Vehicle's statutory capital surplus as of December 31, 2010 were approximately $18.7 million and $22.0 million, respectively, and their statutory net losses in 2010 were $12.0 million and $1.6 million, respectively.

As of December 31, 2011, 2010, and 2009, we did not have any relationships with unconsolidated entities or financial partnerships, such as entities often referred to as "structured finance" or "special purpose" entities, which were established for the purpose of facilitating off-balance-sheet arrangements or other contractually narrow or limited purposes. As such, management believes that we currently are not exposed to any financing, liquidity, market or credit risks that could arise if we had engaged in transactions of that type requiring disclosure herein.

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21st Century Holding Company
Management's Discussion and Analysis of Financial Condition and Results of Operations

IMPACT OF INFLATION AND CHANGING PRICES

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

Insurance premiums are established before we know the amount of losses and LAE and the extent to which inflation may affect such expenses. Consequently, we attempt to anticipate the future impact of inflation when establishing rate levels. While we attempt to charge adequate premiums, we may be limited in raising premium levels for competitive and regulatory reasons. Inflation may also affect the market value of our investment portfolio and the investment rate of return. Any future economic changes that result in prolonged and increasing levels of inflation could cause increases in the dollar amount of incurred losses and LAE and thereby materially adversely affect future liability requirements.

SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	Year Ended December 31, 2011 (Dollars in Thousands except EPS)			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue:				
Net premiums earned	$11,144	$11,660	$12,892	$12,827
Other revenue	1,982	2,516	3,302	3,840
Total revenue	13,126	14,176	16,194	16,667
Expenses:				
Losses and LAE	8,447	7,818	7,852	6,779
Other expenses	7,852	7,474	7,800	7,141
Total expenses	16,299	15,292	15,652	13,920
(Loss) income before provision for income tax (benefit) expense	(3,173)	(1,116)	542	2,747
Provision for income tax (benefit) expense	(1,166)	(311)	114	793
Net (loss) income	$(2,007)	$(805)	$428	$1,954
Basic net (loss) income per share	$(0.25)	$(0.10)	$0.05	$0.25
Fully diluted net (loss) income per share	$(0.25)	$(0.10)	$0.05	$0.25
Weighted average number of common shares outstanding	7,946	7,946	7,946	7,946

Weighted average number of common shares outstanding (assuming dilution)	7,946	7,946	7,946	7,946

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21st Century Holding Company
Management's Discussion and Analysis of Financial Condition and Results of Operations

	Year Ended December 31, 2010 (Dollars in Thousands except EPS)			
	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Revenue:				
Net premiums earned	$11,016	$10,892	$11,621	$11,531
Other revenue	4,764	4,142	3,858	2,780
Total revenue	15,780	15,034	15,479	14,311
Expenses:				
Losses and LAE	9,063	10,196	8,669	12,160
Other expenses	8,249	8,224	8,601	7,397
Total expenses	17,312	18,420	17,270	19,557
Loss before provision for income tax benefit	(1,532)	(3,386)	(1,791)	(5,246)
Provision for income tax benefit	(605)	(1,037)	(523)	(1,794)
Net loss	$(927)	$(2,349)	$(1,268)	$(3,452)
Basic net loss per share	$(0.12)	$(0.30)	$(0.16)	$(0.43)
Fully diluted net loss per share	$(0.12)	$(0.30)	$(0.16)	$(0.43)
Weighted average number of common shares outstanding	7,946	7,946	7,946	7,946
Weighted average number of common shares outstanding (assuming dilution)	7,946	7,946	7,946	7,946

OFF BALANCE SHEET TRANSACTIONS

For the years ended December 31, 2011 and 2010, we had no off balance sheet transactions.

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21st Century Holding Company

ITEM 7A QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

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

Our investment policy is established by the Board of Directors Investment Committee and is reviewed on a regular basis. Pursuant to this investment policy, as of December 31, 2011, approximately 88% of investments were in debt securities and cash and cash equivalents, which are considered to be either held until maturity or available for sale, based upon our estimates of required liquidity. Approximately 94% of the debt securities are considered available for sale and are marked to market. We may in the future consider additional debt securities to be held to maturity and carried at amortized cost. We do not use any swaps, options, futures or forward contracts to hedge or enhance our investment portfolio.

The following table provides information about the financial instruments as of December 31, 2011 that are sensitive to changes in interest rates. The table presents principal cash flows and the related weighted average interest rate by expected maturity date based upon par values.

	2012	2013	2014	2015	2016	Thereafter	Total	Carrying Amount
Principal amount by expected maturity:								
United States government obligations and authorities	$2,000	$1,798	$863	$-	$1,735	$ 12,503	$18,899	$21,206
Obligations of states and political subdivisions	300	350	-	-	-	1,505	2,155	2,303
Corporate securities	5,755	2,308	6,567	4,061	6,685	29,655	55,031	61,011
International securities	-	182	-	-	247	974	1,403	1,524
Collateralized mortgage obligations	154	1,252	13,763	4,731	2,467	1,499	23,866	25,395
Equity securities, at market	-	-	-	-	-	-	-	18,028
All investments	$8,209	$5,890	$21,193	$8,792	$11,134	$ 46,136	$101,354	$129,467

Weighted average interest rate by expected maturity:							
United States government obligations and authorities	4.38 %	3.31 %	1.21 %	0.00 %	1.64 %	3.48 %	3.75 %
Obligations of states and political subdivisions	5.50 %	2.04 %	0.00 %	0.00 %	0.00 %	4.87 %	5.26 %
Corporate securities	3.64 %	3.46 %	5.46 %	4.30 %	3.84 %	6.05 %	5.60 %
International securities	0.00 %	2.25 %	0.00 %	0.00 %	2.38 %	4.85 %	4.08 %
Collateralized mortgage obligations	4.50 %	4.89 %	4.78 %	4.53 %	5.50 %	4.41 %	4.81 %
Equity securities, at market	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %	0.00 %
All investments	3.90 %	3.60 %	4.85 %	4.42 %	3.83 %	5.24 %	5.04 %

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21st Century Holding Company

ITEM 8 FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

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21st Century Holding Company and Subsidiaries

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

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

We have audited the accompanying consolidated balance sheets of 21st Century Holding Company as of December 31, 2011 and 2010, and the related consolidated statements of income, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended December 31, 2011. 21st Century Holding Company's management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of 21st Century Holding Company as of December 31, 2011 and 2010, and the results of its operations and its cash flows for each of the years in the three-year period ended December 31, 2011 in conformity with accounting principles generally accepted in the United States of America.

De Meo Young McGrath

Boca Raton, FL

March 30, 2012

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21st Century Holding Company and Subsidiaries
CONSOLIDATED BALANCE SHEETS
DECEMBER 31, 2011 AND 2010

	Period Ending	
	December 31, 2011	December 31, 2010
ASSETS	(Dollars in Thousands)	
Investments		
Debt maturities, available for sale, at fair value	$104,311	$98,350
Debt maturities, held to maturity, at amortized cost	7,128	6,198
Equity securities, available for sale, at fair value	18,028	17,937
Total investments	129,467	122,485
Cash and short term investments	15,205	16,206
Prepaid reinsurance premiums	8,339	10,416
Premiums receivable, net of allowance for credit losses of $73 and $68, respectively	5,616	5,639
Reinsurance recoverable, net	2,087	8,038
Deferred policy acquisition costs	7,718	7,879
Deferred income taxes, net	8,612	7,916
Income taxes receivable	-	2,393
Property, plant and equipment, net	842	767
Other assets	2,094	2,310
Total assets	$179,980	$184,049
LIABILITIES AND SHAREHOLDERS' EQUITY		
Unpaid losses and LAE	$59,983	$66,529
Unearned premiums	47,933	47,136
Premiums deposits and customer credit balances	2,804	2,364
Bank overdraft	7,930	7,430
Income taxes payable	77	-
Deferred gain from sale of property	-	506
Accounts payable and accrued expenses	3,109	2,153
Total liabilities	121,836	126,118
Shareholders' equity:		
Common stock, $0.01 par value. Authorized 25,000,000 shares; issued and outstanding 7,946,384 and 7,946,384, respectively.	79	79
Preferred stock, $0.01 par value. Authorized 1,000,000 shares; none issued or outstanding	-	-
Additional paid-in capital	50,940	50,654
Accumulated other comprehensive income	877	520
Retained earnings	6,248	6,678
Total shareholders' equity	58,144	57,931
Total liabilities and shareholders' equity	$179,980	$184,049

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries
CONSOLIDATED STATEMENTS OF OPERATIONS
YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

	Twelve Months Ended December 31,		
	2011	2010	2009
	(Dollars in Thousands except EPS and share and dividend data)		
Revenue:			
Gross premiums written	$98,269	$96,410	$104,379
Gross premiums ceded	(46,293)	(52,963)	(56,217)
Net premiums written	51,976	43,447	48,162
(Decrease) Increase in prepaid reinsurance premiums	(2,656)	(2,108)	10,163
(Increase) Decrease in unearned premiums	(797)	3,721	(10,349)
Net change in prepaid reinsurance premiums and unearned premiums	(3,453)	1,613	(186)
Net premiums earned	48,523	45,060	47,976
Commission income	994	1,388	1,362
Finance revenue	518	395	294
Managing general agent fees	1,583	1,609	1,620
Net investment income	4,079	3,726	3,397
Net realized investment gains	2,725	6,777	1,117
Regulatory assessments recovered	109	857	2,333
Other income	1,632	792	755
Total revenue	60,163	60,604	58,854
Expenses:			
Losses and LAE	30,896	40,088	43,706
Operating and underwriting expenses	9,916	10,835	9,681
Salaries and wages	8,004	8,611	7,930
Policy acquisition costs - amortization	12,347	13,025	13,747
Total expenses	61,163	72,559	75,064
Loss before provision for income tax benefit	(1,000)	(11,955)	(16,210)
Provision for income tax benefit	(570)	(3,959)	(5,921)
Net loss	$(430)	$(7,996)	$(10,289)
Net loss per share - basic	$(0.05)	$(1.01)	$(1.29)
Net loss per share - diluted	$(0.05)	$(1.01)	$(1.29)
Weighted average number of common shares outstanding - basic	7,946,384	7,946,384	8,002,365

Weighted average number of common shares outstanding - diluted	7,946,384	7,946,384	8,002,365
Dividends paid per share	$-	$0.06	$0.36

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY AND COMPREHENSIVE LOSS
YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

	Comprehensive Loss	Common Stock	Additional Paid-in Capital	Accumulated Other Comprehensive Deficit	Retained Earnings	Total Shareholder's Equity
	(Dollars in Thousands)					
Balance as of December 31, 2008		$80	$49,980	$ (1,189)	$27,360	$ 76,231
Net loss	$(10,289)				(10,289)	(10,289)
Cash dividends					(1,920)	(1,920)
Treasury stock acquired		(1)	(288)			(289)
Stock options exercised						
Shares based compensation			493			493
Net unrealized change in investments, net of tax effect of $1939	3,214			3,214		3,214
Comprehensive loss	$(7,075)					
Balance as of December 31, 2009		$79	$50,185	$ 2,025	$15,151	$ 67,440
Net loss	$(7,996)				(7,996)	(7,996)
Cash dividends					(477)	(477)
Treasury stock acquired						
Shares based compensation			469			469
Net unrealized change in investments, net of tax effect of $909	(1,505)			(1,505)		(1,505)
Comprehensive loss	$(9,501)					
Balance as of December 31, 2010		$79	$50,654	$ 520	$6,678	$ 57,931
Net loss	$(430)				(430)	(430)
Cash dividends						
Treasury stock acquired						
Shares based compensation			286			286
Net unrealized change in investments,net of tax effect	357			357		357

of $215						
Comprehensive loss	$(73)					
Balance as of December 31, 2011		$79	$50,940	$ 877	$6,248	$ 58,144

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

	For the Years Ended December 31,		
	2011	2010	2009
	(Dollars in Thousands)		
Cash flow from operating activities:			
Net loss	$(430)	$(7,996)	$(10,289)
Adjustments to reconcile net loss to net cash provided (used) by operating activities:			
Amortization of investment premium discount, net	1,249	1,039	642
Depreciation and amortization of property plant and equipment, net	168	221	188
Net realized investment gains	(2,725)	(6,777)	(1,117)
Provision for credit losses, net	18	23	30
(Recovery) provision for uncollectible premiums receivable	(5)	(44)	97
Non-cash compensation	263	431	333
Changes in operating assets and liabilities:			
Premiums receivable	29	4,716	(7,055)
Prepaid reinsurance premiums	2,076	(96)	(4,783)
Reinsurance recoverable, net	5,951	7,264	1,578
Income taxes recoverable	2,393	4,676	(4,794)
Deferred income tax expense, net of other comprehensive income	(912)	(2,332)	1,916
Policy acquisition costs, net of amortization	161	388	(1,709)
Other assets	(308)	837	(1,710)
Unpaid losses and LAE	(6,547)	(4,081)	5,835
Unearned premiums	797	(3,721)	10,343
Premium deposits and customer credit balances	441	234	429
Income taxes payable	77	-	-
Bank overdraft	498	(821)	(442)
Accounts payable and accrued expenses	956	(440)	(1,106)
Net cash provided (used) by operating activities	4,150	(6,479)	(11,614)
Cash flow used by investing activities:			
Proceeds from sale of investment securities	108,318	149,025	59,227
Purchases of investment securities available for sale	(113,251)	(153,969)	(141,753)
Purchases of property and equipment	(243)	(130)	(193)
Net cash used by investing activities	(5,176)	(5,074)	(82,719)
Cash flow provided (used) by financing activities:			
Dividends paid	-	(477)	(1,920)
Acquisition of common Stock	-	-	(288)
Tax benefit related to non-cash compensation	25	39	160
Net cash provided (used) by financing activities	25	(438)	(2,048)
Net decrease in cash and short term investments	(1,001)	(11,991)	(96,380)
Cash and short term investments at beginning of period	16,206	28,197	124,577
Cash and short term investments at end of period	$15,205	$16,206	$28,197

See accompanying notes to consolidated financial statements.

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21st Century Holding Company and Subsidiaries
CONSOLIDATED STATEMENTS OF CASH FLOWS
YEARS ENDED DECEMBER 31, 2011, 2010 AND 2009

(continued)	For the Years Ended December 31, 2011	2010	2009
	(Dollars in Thousands)		
Supplemental disclosure of cash flow information:			
Income taxes	$-	$-	$178
Non-cash investing and finance activities:			
Accrued dividends payable	$-	$-	$477

See accompanying notes to consolidated financial statements.

21st Century Holding Company and Subsidiaries
Notes to Consolidated Financial Statements
December 31, 2011

(1) ORGANIZATION AND BUSINESS

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

21st Century is an insurance holding company that controls substantially all steps in the insurance underwriting, distribution and claims processes through our subsidiaries and our contractual relationships with our independent agents and general agents.

We are authorized to underwrite, and/or place through our wholly owned subsidiaries, homeowners, commercial general liability, personal and commercial automobile, personal umbrella, fire, allied lines, workers' compensation and commercial inland marine insurance in Florida and various other states. We are authorized to underwrite in various states on behalf of our wholly owned subsidiary, Federated National and other insurance carriers. Federated National is the resulting entity following the merger of Federated National with and into our other wholly owned subsidiary, American Vehicle in January 2011.In connection with this merger, the Company, Federated National and American Vehicle entered into the Consent Order with the Florida OIR. See "Footnote 8 – Regulatory Requirements and Restrictions". We market and distribute our own and third-party insurers' products and our other services through a network of independent agents. We also utilize a select number of general agents for the same purpose.

The insurable events during 2011, 2010 and 2009 did not include any weather related catastrophic events such as the well publicized series of hurricanes that occurred in Florida during 2005 and 2004. During 2011, 2010 and 2009 we processed property and liability claims stemming from our homeowners', commercial general liability and private passenger automobile lines of business. Our reinsurance strategy serves to smooth the liquidity requirements imposed by most severe insurable events and for all other insurable events we manage, at a micro and macro perspective, in the normal course of business.

We are not certain how hurricanes and other insurable events will affect our future results of operations and liquidity. Loss and loss adjustment expenses ("LAE") are affected by a number of factors including the following.

- the quality of the insurable risks underwritten;
- the nature and severity of the loss;
- weather-related patterns;
- the availability, cost and terms of reinsurance;
- underlying settlement costs, including medical and legal costs;
- legal and political factors such as legislative initiatives and public opinion;
- macroeconomic issues.

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

Federated National is licensed as an admitted carrier in Florida. Through contractual relationships with a network of approximately 3,000 independent agents, of which approximately 600 actively sell and service our products, Federated National is authorized to underwrite homeowners', fire, allied lines and personal and commercial automobile insurance in Florida. Effective January 26, 2011, Federated National merged with and into American Vehicle and American Vehicle changed its name to Federated National.

American Vehicle, prior to the January 2011 merger, was licensed as an admitted carrier in Florida, and underwrote commercial general liability, and personal and commercial automobile insurance. American Vehicle was also licensed as an admitted carrier in Alabama, Louisiana, Georgia and Texas, and underwrote commercial general liability insurance in those states. American Vehicle operated as a non-admitted carrier in Arkansas, California, Kentucky, Maryland, Missouri, Nevada, Oklahoma, South Carolina, Tennessee and Virginia, and could underwrite commercial general liability insurance in all of these states. Subsequent to the merger, these operations may continue under the newly formed Federated National.

An admitted carrier is an insurance company that has received a license from the state department of insurance giving the company the authority to write specific lines of insurance in that state. These companies are also bound by rate and form regulations, and are strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud. Admitted carriers are also required to financially contribute to the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due their policyholders.

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A non-admitted carrier is allowed to do business in that state and is strictly regulated to protect policyholders from a variety of illegal and unethical practices, including fraud. Sometimes, non-admitted carriers are referred to as “excess and surplus” lines carriers. Non-admitted carriers are subject to considerably less regulation with respect to policy rates and forms. Non-admitted carriers are not required to financially contribute to and benefit from the state guarantee fund, which is used to pay for losses if an insurance carrier becomes insolvent or unable to pay the losses due their policyholders.

During 2008 Federated National applied for and was granted, by the Florida OIR, a license to underwrite fire and allied lines insurance as an admitted carrier. Operations under Federated National’s allied lines began in 2008 as a cedant for the insurance policies it underwrites to the federal flood program. Operations under Federated National’s granted fire line of business began in 2009.

During 2007 American Vehicle applied for and was granted, by the Florida OIR in 2008, a license to underwrite commercial multi-peril and inland marine lines of business as an admitted carrier. Operations under American Vehicle’s newly granted lines of authority began in 2009.

During 2011, 81.8%, 10.3%, 4.6% and 3.3% of the premiums we underwrote were for homeowners’, commercial general liability, federal flood, and personal automobile insurance, respectively. During 2010, 79.7%, 12.3%, 4.1% and 3.9% of the premiums we underwrote were for homeowners’, commercial general liability, federal flood, and personal automobile insurance, respectively.

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. When our estimated liabilities for unpaid losses and LAE are less than the actuarially determined amounts, we increase the expense in the current period. Conversely, when our estimated liabilities for unpaid losses and LAE are greater than the actuarially determined amounts, we decrease the expense in the current period.

We internally process claims made by our insureds through our wholly owned claims adjusting company, Superior. Until June 2011, we offered premium financing to our own and third-party insureds through our wholly owned subsidiary, Federated Premium.

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

Assurance MGA, a wholly owned subsidiary of the Company, acts as Federated National’s exclusive managing general agent in Florida and is also licensed as a managing general agent in the States of Alabama, Arkansas, Georgia, Illinois, Louisiana, North Carolina, Mississippi, Missouri, New York, Nevada, South Carolina, Texas and Virginia. Assurance MGA has contracted with several unaffiliated insurance companies to sell commercial general liability, workers compensation, personal umbrella and inland marine insurance through Assurance MGA’s existing network of agents.

Assurance MGA earns commissions and fees for providing policy administration, marketing, accounting and analytical services, and for participating in the negotiation of reinsurance contracts. Assurance MGA earns a $25 per policy fee, and traditionally a 6% commission fee from its affiliates Federated National and American Vehicle. During the fourth quarter of 2010, Assurance MGA, pursuant to the Consent Order as discussed in "Footnote 8 - Regulation – Consent Order" reduced its fee, to earn amounts varying between 2% and 4%, which we anticipate will return to 6% at an unknown future date with approval from the Florida OIR. A formal agreement reflecting this fee modification was executed during January 2011.

The homeowner policy provides Assurance MGA the right to cancel any policy within a period of 90 days from the policy's inception with 25 days' notice, or after 90 days from policy inception with 95 days' notice, even if the risk falls within our underwriting criteria.

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(2) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND PRACTICES

(a) CASH AND SHORT TERM INVESTMENTS

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

(b) INVESTMENTS

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

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

(c) PREMIUM REVENUE

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

(d) DEFERRED ACQUISITION COSTS

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

(e) PREMIUM DEPOSITS

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

(f) UNPAID LOSSES AND LAE

Unpaid losses and LAE are determined by establishing liabilities in amounts estimated to cover incurred losses and LAE. Such liabilities are determined based upon our assessment of claims pending and the development of prior years' loss liability. These amounts include liabilities based upon individual case estimates for reported losses and LAE and estimates of such amounts that are IBNR. Changes in the estimated liability are charged or credited to operations as the losses and LAE are settled.

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

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

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

We do not discount unpaid losses and LAE for financial statement purposes.

(g) FINANCE REVENUE

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

(h) PREMIUMS RECEIVABLE, NET OF ALLOWANCE FOR CREDIT LOSSES

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

(i) MANAGING GENERAL AGENT (“MGA”) FEES

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

companies and passed through to Assurance MGA. Policy fees are discussed below.

(j) POLICY FEES

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

(k) REINSURANCE

We recognize the income and expense on reinsurance contracts principally on a pro-rata basis over the term of the reinsurance contracts or until the reinsurers maximum liability is exhausted, whichever comes first. We are reinsured under separate reinsurance agreements for the different lines of business underwritten. Reinsurance contracts do not relieve us from our obligations to policyholders. We continually monitor our reinsurers to minimize our exposure to significant losses from reinsurer insolvencies. We only cede risks to reinsurers whom we believe to be financially sound. At December 31, 2011, all reinsurance recoverables are considered current and deemed collectable.

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(l) INCOME TAXES

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

(m) CONCENTRATION OF CREDIT RISK

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

(n) RECENT ACCOUNTING PRONOUNCEMENTS

In December 2011, the FASB issued Accounting Standard Update (“ASU”) No. 2011-12: Comprehensive Income (Topic 220): Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05. The guidance defers certain provisions contained in ASU No. 2011-05 requiring the requirement to present components of reclassifications of other comprehensive income on the face of the income statement or in the notes to the financial statements. However, this deferral does not impact the other requirements contained in the new standard on comprehensive income as described above. This ASU is effective during interim and annual periods beginning after December 15, 2011. The adoption of this ASU will not have a material impact on our financial condition, results of operations or cash flows.

In June 2011, the FASB issued ASU No. 2011-05: Comprehensive Income (Topic 220): Presentation of Comprehensive Income. The guidance in this ASU is intended to increase the prominence of items reported in other comprehensive income in the financial statements by presenting the total of comprehensive income, the components of net income and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. This ASU eliminates the option to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. The guidance in this ASU does not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. Upon adoption, this update is to be applied retrospectively and is effective during interim and annual periods beginning after December 15, 2011. Early adoption is permitted. The adoption of this ASU will not have a material impact on our financial condition, results of operations or cash flows.

In September 2011, the FASB issued ASU No. 2011-08: Intangibles – Goodwill and Other (Topic 350): Testing Goodwill for Impairment, which amends ASC Topic 350, Intangibles-Goodwill and Other. The guidance in this ASU permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test described in ASC Topic 350. Under the amendments in this ASU, an entity is not required to calculate the fair value of a reporting unit unless the entity determines that it is more likely than not that its fair value is less than its carrying amount. The amendments are effective for annual and interim goodwill impairment tests performed for fiscal years beginning after December 15, 2011. Early adoption is permitted, including for annual and interim goodwill impairment tests performed as of a date before September 15, 2011, if an entity's financial statements for the most recent annual or interim period have not yet been issued or, for nonpublic entities, have not yet been made available for issuance. The adoption of this ASU will not have a material impact on our financial condition, results of operations or cash flows.

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In December 2011, the FASB issued ASU No. 2011-11: Balance Sheet (Topic 210): Disclosures about Offsetting Assets and Liabilities, which requires new disclosure requirements mandating that entities disclose both gross and net information about instruments and transactions eligible for offset in the statement of financial position as well as instruments and transactions subject to an agreement similar to a master netting arrangement. In addition, the standard requires disclosure of collateral received and posted in connection with master netting agreements or similar arrangements. This ASU is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The adoption of this ASU will not have a material impact on our financial condition, results of operations or cash flows.

In December 2010, the FASB issued ASU No. 2010-29: Business Combinations (Topic 805): Disclosure of Supplementary Pro Forma Information for Business Combinations a consensus of the FASB Emerging Issues Task Force. The objective of this update is to address diversity in practice about the interpretation of the pro forma revenue and earnings disclosure requirements for business combinations. Paragraph 805-10-50-2(h) requires a public entity to disclose pro forma information for business combinations that occurred in the current reporting period. The disclosures include pro forma revenue and earnings of the combined entity for the current reporting period as though the acquisition date for all business combinations that occurred during the year had been as of the beginning of the annual reporting period. If comparative financial statements are presented, the pro forma revenue and earnings of the combined entity for the comparable prior reporting period should be reported as though the acquisition date for all business combinations that occurred during the current year had been as of the beginning of the comparable prior annual reporting period. In practice, some preparers have presented the pro forma information in their comparative financial statements as if the business combination that occurred in the current reporting period had occurred as of the beginning of each of the current and prior annual reporting periods. Other preparers have disclosed the pro forma information as if the business combination occurred at the beginning of the prior annual reporting period only, and carried forward the related adjustments, if applicable, through the current reporting period. The amendments in this update are effective prospectively for business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after December 15, 2010. The adoption of this update did not have a material impact on the Company’s financial statements.

In October 2010, the FASB issued ASU No. 2010-26: Financial Services – Insurance (Topic 944): Accounting for Costs Associated with Acquiring or Renewing Insurance Contracts, a consensus of FASB Emerging Issues Task Force. The amendments in this update modify the definition of the types of costs incurred by insurance entities that can be capitalized in the acquisition of new and renewal contracts. The amendments in this update specify that the costs must be based on successful efforts (that is, acquiring a new or renewal contract). The amendments also specify that advertising costs should be included as deferred acquisition costs under certain circumstances. The amendments in this update are effective for fiscal years, and interim period within those fiscal years, beginning after December 15, 2011. The amendments in this update should be applied prospectively upon adoption. Retrospective application to all prior periods presented upon the date of adoption also is permitted, but not required. Early adoption is permitted, but only at the beginning of an entity’s annual reporting period. The adoption of this ASU is not expected to have a material impact on the Company’s consolidated financial statements.

In February 2010, the FASB issued ASU No. 2010-09: Amendments to Certain Recognition and Disclosure Requirements, an amendment to Topic 855 Subsequent Events, to address potentially conflicting interactions of the requirements in this Topic with the SEC’s reporting requirements. This update amends Topic 855 as follows: i) an entity that either is a SEC filer or a conduit bond obligor is required to evaluate subsequent events through the date that the financial statements are issued, if the entity does not meet either of these criteria then it should evaluate

subsequent events through the date the financial statements are available to be issued; and ii) an SEC filer is not required to disclose the date through which subsequent events have been evaluated. All amendments in this ASU are effective upon issuance of this ASU, except for the use of the issued date for conduit debt obligors which effective date is for interim and annual periods ending after June 15, 2010. The Company's subsequent events disclosure reflects the new guidance.

In January 2010, the FASB issued ASU No. 2010-06: Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements. The amendments in ASU 2010-06 require additional disclosures about fair value measurements, including transfers in and out of Levels 1 and 2 and activity in Level 3 on a gross basis, and clarifies certain other existing disclosure requirements including level of disaggregation and disclosures around inputs and valuation techniques. The provisions of the new standards are effective for interim or annual reporting periods beginning after December 15, 2009, except for the additional Level 3 disclosures, which will become effective for fiscal years beginnings after December 15, 2010. These standards are disclosure only in nature and do not change accounting requirements. Accordingly, adoption of the new standard had no impact on the Company's consolidated financial position, results of operations or cash flows.

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Other recent accounting pronouncements issued by the FASB, the American Institute of Certified Public Accountants ("AICPA"), and the Securities and Exchange Commission ("SEC") did not or are not believed by management to have a material impact on the Company's present or future financial statements.

(o) USE OF ESTIMATES

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

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

(p) OPERATIONAL RISKS

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

Risks Related to Our Business

Effective January 26, 2011, Federated National merged with and into American Vehicle, and the resulting entity changed its name to "Federated National Insurance Company".

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

- We have exhausted the reinsurance coverage available for Hurricane Wilma and if any claims exceed this coverage amount, it could adversely impact our business, results of operations and/or financial condition.

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

- We face a risk of non-collectibility of reinsurance, which could materially and adversely affect our business, results of operations and/or financial condition.

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

- We may require additional capital in the future which may not be available or only available on unfavorable terms.
- Our business is heavily regulated, and changes in regulation may reduce our profitability and limit our growth.
- We may experience financial exposure from climate change.
- Our loss reserves may be inadequate to cover our actual liability for losses, causing our results of operations to be adversely affected.

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- Our revenues and operating performance may fluctuate due to statutorily approved assessments that support property and casualty insurance pools and associations.
- Our investment portfolio may suffer reduced returns or losses, which would significantly reduce our earnings.
- We may experience a loss due to the concentration of credit risk.
- We face risks in connection with potential material weakness resulting from our Sarbanes-Oxley Section 404 management report and any related remedial measures that we undertake.
- The failure of any of the loss limitation methods we employ could have a material adverse effect on our financial condition or our results of operations.
- The effects of emerging claim and coverage issues on our business are uncertain.
- Our failure to pay claims accurately could adversely affect our business, financial results and capital requirements.
- Our insurance companies are subject to minimum capital and surplus requirements, and our failure to meet these requirements could subject us to regulatory action.
- Our revenues and operating performance may fluctuate with business cycles in the property and casualty insurance industry.
- We may not obtain the necessary regulatory approvals to expand the types of insurance products we offer or the states in which we operate.
- Adverse ratings by insurance rating agencies may adversely impact our ability to write new policies, renew desirable policies or obtain adequate insurance, which could limit or halt our growth and harm our business.
- We rely on independent and general agents to write our insurance policies, and if we are not able to attract and retain independent and general agents, our revenues would be negatively affected.
- We rely on our information technology and telecommunications systems, and the failure of these systems could disrupt our operations.
- Nonstandard automobile insurance historically has a higher frequency of claims than standard automobile insurance, thereby increasing our potential for loss exposure beyond what we would be likely to experience if we offered only standard automobile insurance.
- Florida's personal injury protection insurance statute contains provisions that favor claimants, causing us to experience a higher frequency of claims than might otherwise be the case if we operated only outside of Florida.
- Our success depends on our ability to accurately price the risks we underwrite.
- Current operating resources are necessary to develop future new insurance products.

- Increased competition, competitive pressures, industry developments and market conditions could affect the growth of our business and adversely impact our financial results.

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

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Risks Related to an Investment in Our Shares

- We have authorized but unissued preferred stock, which could affect rights of holders of common stock.
- Our articles of incorporation, bylaws and Florida law may discourage takeover attempts and may result in entrenchment of management.
- As a holding company, we depend on the earnings of our subsidiaries and their ability to pay management fees and dividends to the holding company as the primary source of our income.

(q) FAIR VALUE

The fair value of our investments is estimated based on prices published by financial services or quotations received from securities dealers and is reflective of the interest rate environment that existed as of the close of business on December 31, 2011 and 2010. Changes in interest rates subsequent to December 31, 2011 may affect the fair value of our investments. Refer to Footnote 21 of the Notes to Consolidated Financial Statements for details.

The carrying amounts for the following financial instrument categories approximate their fair values at December 31, 2011 and 2010 because of their short-term nature: cash and short term investments, premiums receivable, finance contracts, due from reinsurers, revolving credit outstanding, bank overdraft, accounts payable and accrued expenses.

(r) STOCK OPTION PLANS

During the year ended December 31, 2011, the Company had two stock-based employee compensation plans, which are described later in Footnote 14, Stock Compensation Plans. Prior to January 1, 2006, we accounted for the plans under the recognition and measurement provisions of stock-based compensation using the intrinsic value method prescribed by the Accounting Principles Board ("APB") and related Interpretation, as permitted by FASB issued guidance. Under these provisions, no stock-based employee compensation cost was recognized in the Statement of Operations as all options granted under those plans had an exercise price equal to or less than the market value of the underlying common stock on the date of grant.

Effective January 1, 2006, the Company adopted the fair value recognition provisions of FASB issued guidance using the modified-prospective-transition method. Under that transition method, compensation costs recognized during 2011, 2010 and 2009 include:

- Compensation cost for all share-based payments granted prior to, but not yet vested as of January 1, 2006, based on the grant date fair value estimated in accordance with the original provisions of FASB issued guidance, and
- Compensation cost for all share-based payments granted subsequent to January 1, 2006, based on the grant-date fair-value estimated in accordance with the provisions of FASB issued guidance. Results for prior periods have not been restated, as they are not required to be by the pronouncement.

(s) PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment is stated at cost less accumulated depreciation. Depreciation on property, plant and equipment is calculated on a straight-line basis over the following estimated useful lives: building and improvements - 30 years and furniture and fixtures - 7 years. We capitalize betterments and any other expenditure in excess of $1,000 if the asset is expected to have a useful life greater than one year. The carrying value of property, plant and equipment is periodically reviewed based on the expected future undiscounted operating cash flows of the related item. Based upon our most recent analysis, we believe that no impairment of property, plant and equipment exists at December 31, 2011.

(t) RECLASSIFICATIONS

Certain 2010 and 2009 financial statement amounts have been reclassified to conform to the 2011 presentations.

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(u) GOODWILL AND INTANGIBLE ASSETS

During 2009, the Company purchased one intangible asset totaling $0.1 million. In accordance with FASB issued guidance, the accounting for the recognized intangible asset was based on its useful life to the Company. The useful life of the intangible asset was the period over which it was expected to contribute directly or indirectly to the future cash flows of the Company. The intangible asset had a definite finite life ranging from six to twelve months, and was amortized accordingly.

(3) INVESTMENTS

FASB issued guidance addresses accounting and reporting for (a) investments in equity securities that have readily determinable fair values and (b) all investments in debt securities. The guidance requires that these securities be classified into one of three categories: Held-to-maturity, Trading, or Available-for-sale securities.

Investments classified as held-to-maturity include debt securities wherein the Company's intent and ability are to hold the investment until maturity. The accounting treatment for held-to-maturity investments is to carry them at amortized cost without consideration to unrealized gains or losses. Investments classified as trading securities include debt and equity securities bought and held primarily for the sale in the near term. The accounting treatment for trading securities is to carry them at fair value with unrealized holding gains and losses included in current period operations. Investments classified as available-for-sale include debt and equity securities that are not classified as held-to-maturity or as trading security investments. The accounting treatment for available-for-sale securities is to carry them at fair value with unrealized holding gains and losses excluded from earnings and reported as a separate component of shareholders' equity, namely "Other Comprehensive Income".

Total Investments increased $7.0 million, or 5.7%, to $129.5 million as of December 31, 2011, compared with $122.5 million as of December 31, 2010.

The debt and equity securities that are available for sale and carried at fair value represent 94% of total investments as of December 31, 2011, compared with 95% as of December 31, 2010.

We did not hold any trading investment securities during 2011.

The FASB issued guidance also addresses the determination as to when an investment is considered impaired, whether that impairment is other-than temporary, and the measurement of an impairment loss. The Company's policy for the valuation of temporarily impaired securities is to determine impairment based on the analysis of the following factors.

- rating downgrade or other credit event (eg., failure to pay interest when due);
- length of time and the extent to which the fair value has been less than amortized cost;
- financial condition and near term prospects of the issuer, including any specific events which may influence the operations of the issuer such as changes in technology or discontinuance of a business segment;
- prospects for the issuer's industry segment;

- intent and ability of the Company to retain the investment for a period of time sufficient to allow for anticipated recovery in market value;
- historical volatility of the fair value of the security.

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

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In reaching a conclusion that a security is either other-than-temporarily or permanently impaired we consider such factors as the timeliness and completeness of expected dividends, principal and interest payments, ratings from nationally recognized statistical rating organizations such as Standard and Poor's and Moody's, as well as information released via the general media channels. During 2011, in connection with this process, we charged to operations $0.8 million of investment losses. During 2010, in connection with this process, we have not charged any net realized investment loss to operations.

As of December 31, 2011 and December 31, 2010, respectively, all of our securities are in good standing and not impaired, except as noted above, as defined by FASB-issued guidance.

As of December 31, 2011 and 2010, our investments consisted primarily of corporate bonds held in various industries, municipal bonds and United States government bonds. As of December 31, 2011, 61% of our debt portfolio was in diverse industries and 39% is in United States government bonds. As of December 31, 2011, approximately 83% of our equity holdings were in equities related to diverse industries and 17% were in mutual funds. As of December 31, 2010, 72% of our debt portfolio was in diverse industries and 28% was in United States government bonds. As of December 31, 2010, approximately 77% of our equity holdings were in equities related to diverse industries and 23% were in mutual funds.

As of December 31, 2011 and December 31, 2010, we have classified $7.1 million and $6.2 million, respectively, of our bond portfolio as held-to-maturity. We only classify bonds as held-to-maturity to support securitization of credit requirements.

During 2011, we did not re-classify any of our bond portfolio between available-for-sale and held-to-maturity.

During 2010, we re-classified $3.1 million of amortized cost to held-to-maturity from available-for-sale to fund trust agreements.

During April 2006, American Vehicle finalized a $15.0 million irrevocable letter of credit in conjunction with the 100% Quota Share Reinsurance Agreement with Republic Underwriters Insurance Company ("Republic") which was terminated in April 2007. During 2010, the letter of credit in favor of Republic was replaced by a fully funded trust agreement. As of December 31, 2011 and 2010 respectively, the amount held in trust was $1.0 million.

(a) DEBT AND EQUITY SECURITIES

The following table summarizes, by type, our investments as of December 31, 2011 and 2010.

	December 31, 2011			December 31, 2010		
	Carrying Amount	Percent of Total		Carrying Amount	Percent of Total	
	(Dollars in Thousands)					
Debt securities, at market:						
United States government obligations and authorities	$37,217	28.75	%	$28,196	23.02	%
Obligations of states and political subdivisions	2,303	1.77	%	2,963	2.42	%
Corporate	63,268	48.87	%	65,808	53.73	%
International	1,523	1.18	%	1,383	1.13	%

	104,311	80.57	%	98,350	80.30	%
Debt securities, at amortized cost:						
Corporate	962	0.74	%	818	0.67	%
United States government obligations and authorities	6,166	4.76	%	5,380	4.39	%
	7,128	5.50	%	6,198	5.06	%
Total debt securities	111,439	86.07	%	104,548	85.36	%
Equity securities, at market:	18,028	13.93	%	17,937	14.64	%
Total investments	$129,467	100.00	%	$122,485	100.00	%

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The following table shows the realized gains (losses) for debt and equity securities for the years ended December 31, 2011 and 2010.

	Years Ended December 31,			
	2011		2010	
	Gains (Losses)	Fair Value at Sale	Gains (Losses)	Fair Value at Sale
	(Dollars in Thousands)			
Debt securities	$3,569	$66,680	$4,484	$98,318
Equity securities	1,240	8,305	4,228	27,898
Total realized gains	4,809	74,985	8,712	126,216
Debt securities	(595)	18,086	(209)	12,295
Equity securities	(1,489)	3,510	(1,726)	8,715
Total realized losses	(2,084)	21,596	(1,935)	21,010
Net realized gains on investments	$2,725	$96,581	$6,777	$147,226

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A summary of the amortized cost, estimated fair value, gross unrealized gains and losses of debt and equity securities at December 31, 2011 and 2010 is as follows.

	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Estimated Fair Value
		(Dollars in Thousands)		
December 31, 2011				
Debt Securities - Available-For-Sale:				
United States government obligations and authorities	$36,558	$686	$27	$37,217
Obligations of states and political subdivisions	2,165	138	-	2,303
Corporate	61,724	1,934	390	63,268
International	1,519	9	5	1,523
	$101,966	$2,767	$422	$104,311
Debt Securities - Held-To-Maturity:				
United States government obligations and authorities	$6,166	$249	$-	$6,415
Corporate	962	39	1	1,000
	$7,128	$288	$1	$7,415
Equity securities - common stocks	$18,966	$1,057	$1,995	$18,028
December 31, 2010				
Debt Securities - Available-For-Sale:				
United States government obligations and authorities	$28,389	$191	$384	$28,196
Obligations of states and political subdivisions	2,920	49	6	2,963
Corporate	65,540	850	581	65,809
International	1,358	25	1	1,382
	$98,207	$1,115	$	