TIERONE CORP
Form 10-Q
August 06, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2004

OR

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

For the transition period from _____ to _____

Commission file number: 000-50015

TierOne Corporation

(Exact name of Registrant as specified in its charter)

Wisconsin	04-3638672
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification No.)
1235 "N" Street Lincoln, Nebraska	68508
(Address of Principal Executive Offices)	(Zip Code)

(402) 475-0521

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such 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. Yes _X_ No _

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes _X_ No _

At August 3, 2004, the registrant had 18,285,811 shares of common stock, $.01 par value per share, outstanding.

PART I - FINANCIAL INFORMATION

TierOne Corporation and Subsidiaries
Consolidated Balance Sheets
June 30, 2004 (Unaudited) and December 31, 2003

(Dollars in thousands, except per share data)	**June 30, 2004**	**December 31, 2003**
ASSETS		
Cash and cash equivalents	$ 34,616	$ 34,901
Investment securities:		
Held to maturity, at cost which approximates fair value	135	142
Available for sale, at fair value	37,678	43,515
Mortgage-backed securities, available for sale, at fair value	12,804	15,712
Loans receivable:		
Net loans (includes loans held for sale of $10,864 and $7,083 at June 30, 2004 and December 31, 2003, respectively)	2,088,846	2,036,182
Allowance for loan losses	(20,886)	(19,586)
Net loans after allowance for loan losses	2,067,960	2,016,596
Federal Home Loan Bank stock	37,792	37,143
Premises and equipment, net	28,975	27,587
Accrued interest receivable	9,477	9,678
Other assets	25,832	22,594

(Dollars in thousands, except per share data)	June 30, 2004	December 31, 2003
Total assets	$ 2,255,269	$ 2,207,868
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities:		
Deposits	$ 1,324,074	$ 1,216,763
Advances from Federal Home Loan Bank and other borrowings	619,752	645,696
Advance payments from borrowers for taxes, insurance and other escrow funds	21,274	22,206
Accrued interest payable	5,166	5,259
Accrued expenses and other liabilities	21,407	22,855
Total liabilities	1,991,673	1,912,779
Shareholders' equity:		
Preferred stock, $0.01 par value. 10,000,000 shares authorized; none issued	--	--
Common stock, $0.01 par value. 60,000,000 shares authorized; 18,285,811 and 20,317,568 shares issued and outstanding at June 30, 2004 and December 31, 2003, respectively	226	226
Additional paid-in capital	355,051	354,054
Retained earnings, substantially restricted	35,699	25,833
Treasury stock, at cost; 4,289,264 and 2,257,507 shares at June 30, 2004 and December 31, 2003	(98,300)	(53,613)
Unallocated common stock held by Employee Stock Ownership Plan	(15,426)	(16,179)
Unearned common stock held by Management Recognition and Retention Plan	(13,618)	(14,982)
Accumulated other comprehensive income (loss), net	(36)	(250)
Total shareholders' equity	263,596	295,089
Commitments and contingent liabilities		
Total liabilities and shareholders' equity	$ 2,255,269	$ 2,207,868

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Income
(Unaudited)

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
(Dollars in thousands, except per share data)	2004	2003	2004	2003
Interest income:				
Loans receivable	$ 27,074	$ 27,373	$ 54,237	$ 54,166
Investment securities	903	1,115	1,830	2,147
Other interest-earning assets	--	--	--	99
Total interest income	27,977	28,488	56,067	56,412

	For the Three Months Ended June 30,		For the Six Months Ended June 30,	
Interest expense:				
Deposits	5,877	5,866	11,532	12,089
Advances from Federal Home Loan Bank and other borrowings	4,965	4,530	9,652	8,594
Total interest expense	10,842	10,396	21,184	20,683
Net interest income	17,135	18,092	34,883	35,729
Provision for loan losses	1,105	515	2,039	1,687
Net interest income after provision for loan losses	16,030	17,577	32,844	34,042
Noninterest income:				
Fees and service charges	4,697	612	7,810	1,579
Income (loss) from real estate operations, net	(32)	26	(109)	8
Net gain on sales of:				
Investment securities	312	--	312	--
Loans held for sale	705	2,653	1,021	4,608
Real estate owned	44	(93)	44	(79)
Gain on pension plan curtailment	--	--	1,456	--
Other operating income	569	695	1,202	1,406
Total noninterest income	6,295	3,893	11,736	7,522
Noninterest expense:				
Salaries and employee benefits	7,808	7,096	15,672	13,415
Occupancy, net	1,551	1,328	3,017	2,759
Data processing	463	407	967	818
Advertising	948	904	1,641	1,628
Other operating expense	2,632	2,007	4,701	4,215
Total noninterest expense	13,402	11,742	25,998	22,835
Income before income taxes	8,923	9,728	18,582	18,729
Income tax expense	3,348	3,593	6,947	6,899
Net income	$ 5,575	$ 6,135	$ 11,635	$ 11,830
Net income per common share, basic	$ 0.33	$ 0.29	$ 0.67	$ 0.57
Net income per common share, diluted	$ 0.32	$ 0.29	$ 0.66	$ 0.57
Dividends declared per common share	$ 0.05	$ -	$ 0.10	$ -
Average common shares outstanding, basic (000's)	16,998	20,828	17,396	20,824
Average common shares outstanding, diluted (000's)	17,283	21,012	17,733	20,929

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Changes in Shareholders Equity and Comprehensive Income
Six Months Ended June 30, 2004 and June 30, 2003
(Unaudited)

(Dollars in thousands)	Common Stock	Additional Paid-In Capital	Retained Earnings, Substantially Restricted	Treasury Stock	Unallocated Common Stock Held by the Employee Stock Ownership Plan	Unearned Common Stock Held by the Management Recognition and Retention Plan	Accumulated Other Comprehensive Income (Loss), Net	Total Shareholders' Equity
Balance at December 31, 2002	$ 226	$ 355,741	$ 2,018	$ --	$ (17,684)	$ --	$ (405)	$ 339,896
Common stock earned by employees in Employee Stock Ownership Plan	--	557	--	--	753	--	--	1,310
Common stock purchased by the Management Recognition and Retention Plan	--	(97)	~	--	--	(1,357)	--	(1,454)
Amortization of awards under the Management Recognition and Retention Plan	--	--	--	--	--	500	--	500
Comprehensive income:								
Net income	--	--	11,830	--	--	--	--	11,830
Change in unrealized loss on available for sale securities, net of tax and reclassification adjustment	--	--	--	--	--	--	20	20
Total comprehensive income	--	--	11,830	--	--	--	20	11,850
Balance at June 30, 2003	$ 226	$ 356,201	$ 13,848	$ --	$ (16,931)	$ (857)	$ (385)	$ 352,102
Balance at December 31, 2003	$ 226	$ 354,054	$ 25,833	$ (53,613)	$ (16,179)	$ (14,982)	$ (250)	$ 295,089
Common stock earned by employees in Employee Stock Ownership Plan	--	914	--	--	753	--	--	1,667
Amortization of awards under the Management Recognition and Retention Plan	--	83	--	--	--	1,364	--	1,447
Repurchase of common stock (2,031,757 shares)				(44,687)				(44,687)
Dividends paid ($0.10 per common share)	--	--	(1,769)	--	--	--	--	(1,769)
Comprehensive income:								
Net income	--	--	11,635	--	--	--	--	11,635
Change in additional minimum pension liability, net of tax	--	--	--	--	--	--	452	452
Change in unrealized gain on available for sale securities, net of tax and reclassification adjustment	--	--	--	--	--	--	(238)	(238)
Total comprehensive income	--	--	11,635	--	--	--	214	11,849
Balance at June 30, 2004	$ 226	$ 355,051	$ 35,699	$ (98,300)	$ (15,426)	$ (13,618)	$ (36)	$ 263,596

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Cash Flows
Six Months Ended June 30, 2004 and June 30, 2003
(Unaudited)

(Dollars in thousands)	**June 30, 2004**	**June 30, 2003**
Reconciliation of net income to net cash provided by operating activities:		
Net income	$ 11,635	$ 11,830
Adjustments to reconcile net income to net cash provided by operating activities:		
Net premium amortization of investment and mortgage-backed securities	115	993
Depreciation and amortization	1,296	1,263
Employee Stock Ownership Plan expense	1,667	1,310
Management Recognition and Retention Plan expense	1,447	500
Amortization of premiums on net loans	4,546	2,286
Federal Home Loan Bank stock dividend	(649)	--
Deferred income tax expense (benefit)	780	12
Provision for loan losses	2,039	1,687
Proceeds from sales of loans held for sale	150,543	311,123
Originations and purchases of loans held for sale	(153,304)	(315,231)
Net (gain) loss on sales of:		
Investment securities	(312)	--
Loans held for sale	(1,021)	(4,608)
Real estate owned	(44)	79
Premises and equipment	4	--
Changes in certain assets and liabilities:		
Accrued interest receivable	201	(241)
Other assets	(2,461)	202
Accrued interest payable	(93)	(914)
Accrued expenses and other liabilities	(1,448)	9,061
Net cash provided by operating activities	14,941	19,352
Cash flows from investing activities:		
Purchase of investment and mortgage-backed securities, available for sale	(11,979)	(101,841)
Proceeds from sale of investment securities, available for sale	13,842	--
Proceeds from maturities of investment securities, available for sale	3,900	2,000
Proceeds from principal repayments of investment and mortgage-backed securities available for sale and held to maturity	2,818	21,027
Increase in loans receivable	(55,842)	(246,575)
Purchase of Federal Home Loan Bank stock	--	(14,009)
Additions to premises and equipment	(3,248)	(2,649)
Proceeds from sale of real estate owned	1,304	2,742
Net cash used in investing activities	(49,205)	(339,305)

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Cash Flows (continued)
Six Months Ended June 30, 2004 and June 30, 2003
(Unaudited)

	June 30,	
(Dollars in thousands)	**2004**	**2003**
Cash flows from financing activities:		
Net increase in deposits	$ 107,311	$ 18,729
Net advances (repayment) on Federal Home Loan Bank line of credit and short-term advances and other borrowings	(56,855)	119,406
Proceeds from Federal Home Loan Bank long-term advances and other borrowings	--	195,000
Repayments of Federal Home Loan Bank long-term advances and other borrowings	(17)	(20,017)
Proceeds from junior subordinated debentures	30,928	--
Net increase (decrease) in advances from borrowers for taxes, insurance and other escrow funds	(932)	3,272
Repurchase of common stock	(44,687)	--
Dividends paid on common stock	(1,769)	--
Purchase of common stock for Management Recognition and Retention Plan	--	(1,454)
Net cash provided by financing activities	33,979	314,936
Net decrease in cash and cash equivalents	(285)	(5,017)
Cash and cash equivalents at beginning of period	34,901	33,037
Cash and cash equivalents at end of period	$ 34,616	$ 28,020
Supplemental disclosures of cash flow information:		
Cash paid during period for:		
Interest	$ 21,277	$ 21,597
Income taxes, net of refunds	$ 6,640	$ 7,491
Noncash investing activities:		
Transfers from loans to real estate owned and other assets through foreclosure	$ 1,675	$ 946

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 Basis of Presentation

TierOne Corporation (the Company) is a Wisconsin corporation headquartered in Lincoln, Nebraska. TierOne Corporation is the holding company for TierOne Bank (the Bank). At June 30, 2004, TierOne Bank operated from 57 banking offices located in Nebraska, Iowa and Kansas, three loan production offices located in Colorado and one loan production office located in Minnesota.

Note 2 Basis of Consolidation

The consolidated financial statements include the accounts of the Bank and its wholly owned subsidiary, TMS Corporation of the Americas (TMS). TMS is the holding company of TierOne Investments and Insurance, Inc., a wholly owned subsidiary that administers the sale of insurance and securities products, and TierOne Reinsurance Company, a wholly owned subsidiary that reinsures credit life and disability insurance policies.

The accompanying interim consolidated financial statements as of June 30, 2004 and for the three and six months ended June 30, 2004 and June 30, 2003 have not been audited by independent auditors. All significant intercompany accounts and transactions have been eliminated in consolidation. In the opinion of management, the accompanying unaudited consolidated financial statements contain all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation. The interim consolidated financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company s Annual Report on Form 10-K for the year ended December 31, 2003. The results of operations for the three and six months ended June 30, 2004 are not necessarily indicative of the results which may be expected for the entire calendar year 2004.

Note 3 Earnings Per Share

Basic and diluted earnings per share (EPS) data are based on the weighted average number of common shares outstanding during each reporting period. Employee Stock Ownership Plan (ESOP) and 2003 Management Recognition and Retention Plan (MRRP) shares not committed to be released are not considered to be outstanding for purposes of EPS calculations. The basic EPS calculation excludes the dilutive effect of all common stock equivalents. Diluted EPS is further adjusted for potential common shares that were dilutive and outstanding during the reporting periods. The Company s potentially dilutive common shares at June 30, 2004 represent shares issuable under its 2003 Stock Option Plan and MRRP computed using the treasury stock method. All stock options awarded are assumed to be 100% vested for purposes of the EPS computations.

	Three Months Ended June 30, 2004		Six Months Ended June 30, 2004	
(Dollars in thousands, except per share data)	**Basic**	**Diluted**	**Basic**	**Diluted**
Net income	$ 5,575	$ 5,575	$ 11,635	$ 11,635
Weighted average number of common shares outstanding used in basic earnings per share calculation (in 000's)	16,998	16,998	17,396	17,396
Common share equivalents - 2003 Stock Option Plan and 2003 Management Recognition and Retentiion Plan shares (in 000's)		285		337

	Three Months Ended June 30, 2004		Six Months Ended June 30, 2004	
Weighted average number of common shares outstanding used in diluted earnings per share calculation (in 000's)		17,283		17,733
Earnings per share	$ 0.33	$ 0.32	$ 0.67	$ 0.66

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 4 Investment and Mortgage-Backed Securities

Investment and mortgage-backed securities at June 30, 2004 and December 31, 2003 are summarized in the following table:

	June 30, 2004			
		Gross Unrealized		
(Dollars in thousands)	Amortized Cost	Gains	Losses	Fair Value
Held to maturity:				
Municipal obligations	$ 135	$ --	$ --	$ 135
Available for sale:				
Mortgage-backed securities	12,686	144	26	12,804
U.S. Government agency obligations	20,958	2	131	20,829
Corporate securities	10,894	78	55	10,917
Asset Management Fund - ARM Fund	6,000	--	68	5,932
Total investment and mortgage-backed securities, available for sale	$ 50,538	$ 224	$ 280	$ 50,482

	December 31, 2003			
		Gross Unrealized		
(Dollars in thousands)	Amortized Cost	Gains	Losses	Fair Value
Held to maturity:				
Municipal obligations	$ 142	$ --	$ --	$ 142
Available for sale:				

	June 30, 2004			
Mortgage-backed securities	15,542	201	31	15,712
U.S. Government agency obligations	12,877	13	4	12,886
Corporate securities	24,496	406	242	24,660
Asset Management Fund - ARM Fund	6,000	--	31	5,969
Total investment and mortgage-backed securities, available for sale	$ 58,915	$ 620	$ 308	$ 59,227

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 5 Loan Portfolio Composition

The following table shows the composition of the Bank s loan portfolio by type of loan at the dates indicated:

	June 30, 2004		December 31, 2003	
(Dollars in thousands)	**Amount**	**%**	**Amount**	**%**
Real estate loans:				
One-to-four family residential (1)	$ 472,072	20.47%	$ 559,134	25.20%
Second mortgage residential	267,811	11.61	258,121	11.63
Multi-family residential	102,677	4.45	99,078	4.47
Commercial real estate and land	453,102	19.64	449,152	20.25
Residential construction	306,621	13.29	245,782	11.08
Commercial construction	193,853	8.40	154,247	6.95
Total real estate loans	1,796,136	77.86	1,765,514	79.58
Business loans	79,199	3.44	64,522	2.91
Warehouse mortgage lines of credit	111,219	4.82	78,759	3.55
Consumer loans:				
Home equity	37,122	1.61	33,874	1.53
Home equity line of credit	128,591	5.57	117,899	5.31
Home improvement	70,344	3.05	74,915	3.38
Automobile	66,514	2.88	67,351	3.04
Other	17,637	0.77	15,621	0.70
Total consumer loans	320,208	13.88	309,660	13.96
Total loans	2,306,762	100.00%	2,218,455	100.00%
Unamortized premiums, discounts and deferred loan fees	8,102		10,790	
Undisbursed portion of construction and				

	June 30, 2004	December 31, 2003
land development loans in process	(226,018)	(193,063)
Net loans	2,088,846	2,036,182
Allowance for loan losses	(20,886)	(19,586)
Net loans after allowance for loan losses	$ 2,067,960	$ 2,016,596
(1) Includes loans held for sale	$ 10,864	$ 7,083

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 6 Allowance for Loan Losses

The following table sets forth the activity in the allowance for loan losses during the periods indicated:

	At or for the Three Months Ended June 30,		At or for the Six Months Ended June 30,	
(Dollars in thousands)	2004	2003	2004	2003
Allowance for loan losses, beginning of period	$ 20,086	$ 17,984	$ 19,586	$ 17,108
Provision for loan losses	1,105	515	2,039	1,687
Charge-offs	(409)	(209)	(916)	(554)
Recoveries on loans previously charged-off	104	36	177	85
Allowance for loan losses, end of period	$ 20,886	$ 18,326	$ 20,886	$ 18,326
Allowance for loan losses as a percentage of net loans	1.00%	0.90%	1.00%	0.90%

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 7 Nonperforming Assets

The following table sets forth information with respect to nonperforming assets and troubled debt restructurings at the dates indicated. It is the Bank s policy to cease accruing interest on loans 90 days or more past due and to charge off accrued interest. Total impaired loans amounted to approximately $1.1 million and $864,000 at June 30, 2004 and December 31, 2003, respectively. There was an allowance for loan loss of $0 and $50,000 specifically allocated to impaired loans at June 30, 2004 and December 31, 2003, respectively.

(Dollars in thousands)	June 30, 2004	December 31, 2003
Non-accruing loans:		
One-to-four family residential	$ 838	$ 1,461
Second mortgage residential	590	224
Multi-family residential	--	--
Commercial real estate and land	--	--
Residential construction	1,207	1,012
Commercial construction	--	--
Business	--	219
Warehouse mortgage lines of credit	--	--
Consumer	909	700
Total non-accruing loans	3,544	3,616
Real estate owned, net (1)	1,093	678
Total nonperforming assets	4,637	4,294
Troubled debt restructurings	1,059	468
Total nonperforming assets and troubled debt restructurings	$ 5,696	$ 4,762
Total nonperforming loans as a percent of net loans	0.17%	0.18%
Total nonperforming assets as a percent of total assets	0.21%	0.19%
Total nonperforming assets and troubled debt restructurings as a percent of total assets	0.25%	0.22%
Allowance for loan losses as a percent of net loans	1.00%	0.96%
Allowance for loan losses as a percent of nonperforming loans	589.33%	541.65%

(1) Real estate owned balances are shown net of related loss allowances. Includes both real property and other repossessed collateral consisting primarily of automobiles.

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TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
(Unaudited)

Note 8 Mortgage Servicing Rights

Mortgage servicing rights are included in the consolidated balance sheets under the caption Other Assets. The activity of mortgage servicing rights during the periods presented is summarized in the following table:

(Dollars in thousands)	Three Months Ended June 30, 2004	Three Months Ended June 30, 2003	Six Months Ended June 30, 2004	Six Months Ended June 30, 2003
Balance at beginning of period	$ 8,691	$ 6,173	$ 8,705	$ 6,290
Mortgage servicing rights capitalized	1,183	2,109	1,795	3,828
Amortization expense	(925)	(1,663)	(1,551)	(2,909)
Valuation adjustment	1,168	(1,366)	1,168	(1,956)
Balance at end of period	$ 10,117	$ 5,253	$ 10,117	$ 5,253

The activity of the valuation allowance on mortgage servicing rights is summarized in the following table for the periods presented:

(Dollars in thousands)	Three Months Ended June 30, 2004	Three Months Ended June 30, 2003	Six Months Ended June 30, 2004	Six Months Ended June 30, 2003
Balance at beginning of period	$ 1,668	$ 2,910	$ 1,668	$ 2,320
Changes in mortgage servicing valuation reserve	(1,168)	1,366	(1,168)	1,956
Balance at end of period	$ 500	$ 4,276	$ 500	$ 4,276

The following table compares the key assumptions used in measuring the fair values of mortgage servicing rights at June 30, 2004 and December 31, 2003:

(Dollars in thousands)	June 30, 2004	December 31, 2003
Serviced loan portfolio balance	$1,009,659	$956,744
Fair value	$11,350	$9,173
Prepayment speed	5.46% - 63.96%	7.56% - 76.44%
Weighted average prepayment speed	13.56%	23.08%
Fair value with 10% adverse change	$10,856	$8,673
Fair value with 20% adverse change	$10,372	$8,218
Discount rate	10.00% - 15.50%	9.00% - 15.00%
Weighted average discount rate	11.58%	10.74%
Fair value with 10% adverse change	$10,925	$8,863
Fair value with 20% adverse change	$10,510	$8,575

Note 9 Stock-Based Benefit Plans

The Company has in effect the MRRP, which is a stock-based incentive plan. The following table summarizes shares of the Company s common stock which were subject to award and were granted in April 2003 pursuant to the MRRP:

	June 30, 2004
Common shares authorized to be awarded by the Management Recognition and Retention Plan	903,003
Common shares awarded by Management Recognition and Retention Plan	(764,850)
Common shares forfeited	--
Shares available for award at June 30, 2004	138,153

The shares awarded under the MRRP vest at the rate of 20% per year. As a result, expense for MRRP awards is being recorded over a 60-month period from the date of grant and is based on the market value of the Company s stock as of the date the awards were made. The remaining unamortized cost of the MRRP shares awarded to date is reflected as a reduction in shareholders equity. Expense under the MRRP for the three and six months ended June 30, 2004 was $682,000 and $1.4 million, respectively, compared to $500,000 for the three and six month periods ended June 30, 2003.

The Company established the 2003 Stock Option Plan (SOP) under which 2,257,508 shares of Company common stock are reserved for issuance pursuant to the grant of stock options to directors, officers and employees. Stock options awarded under the SOP vest at the rate of 20% per year. The exercise price of the options is equal to the fair market value of the common stock on the grant date. At June 30, 2004, 1,852,750 stock options had been granted at an exercise price of $17.83. There were no stock options exercised or forfeited during the three and six months ended June 30, 2004.

At June 30, 2004, 20% of the options granted were exercisable, the weighted-average remaining contractual life of outstanding options was 8.82 years, and there were 404,758 shares remaining available for future grants under the terms of the SOP.

The Company accounts for its stock options in accordance with Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* (APB No. 25). Under the provisions of APB No. 25, since the exercise price of the Company s employees stock options equals the market price of the underlying stock on the date of grant, no compensation expense is recognized. Compensation expense for shares granted under the MRRP is ratably recognized over the period of service, usually the vesting period, based on the fair value of the stock on the date of grant. See Note 13 for a discussion of a proposed new statement issued by the Financial Accounting Standards Board (FASB) which would result in a change in the accounting for equity-based compensation.

Pursuant to FASB Statement No. 123, *Accounting for Stock-Based Compensation* (SFAS No. 123), pro forma net income and pro forma EPS are presented in the following table as if the fair value method of accounting for stock-based compensation plans had been utilized:

	Three Months Ended June 30,		Six Months Ended June 30,	
(Dollars in thousands, except per share data)	**2004**	**2003**	**2004**	**2003**
Net income (as reported)	$ 5,575	$ 6,135	$ 11,635	$ 11,830
Add: stock-based employee compensation expense included in reported net income, net of related tax effects	443	325	887	325
Deduct: total stock-based employee compensation expense determined under				

	Three Months Ended June 30,		Six Months Ended June 30,	
fair value based method for all awards, net of related tax effects	(715)	(524)	(1,430)	(524)
Pro forma net income	$ 5,303	$ 5,936	$ 11,092	$ 11,631
Basic earnings per share (as reported)	$ 0.33	$ 0.29	$ 0.67	$ 0.57
Pro forma basic earnings per share	0.31	0.28	0.64	0.56
Diluted earnings per share (as reported)	0.32	0.29	0.66	0.57
Pro forma diluted earnings per share	0.31	0.28	0.63	0.56

The pro forma results above may not be representative of the effect on net income in future periods.

The fair value of the option grants was estimated using the Black Scholes option value model, with the following assumptions: dividend yield of 1.00%, expected volatility of 13.2%, risk-free interest rate of 3.5% and an original expected life of ten years for all options granted.

TierOne Corporation and Subsidiaries
Notes to Consolidated Financial Statements
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Note 10 Defined Benefit Pension Plan

On March 31, 2004, the Company merged its single-employer defined benefit pension plan and transferred all pension plan assets and future plan obligations to an unrelated third party plan. This transaction resulted in a $1.5 million pre-tax gain for the three months ended March 31, 2004 from the curtailment of the liability associated with the plan.

TierOne Corporation and Subsidiaries
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(Unaudited)

Note 11 Deposits

The following table shows the composition of the Bank s deposits by type at the dates indicated:

	June 30, 2004		December 31, 2003	
(Dollars in thousands)	**Weighted Average Rates**	**Amount**	**Weighted Average Rates**	**Amount**
Transaction accounts:				
Noninterest-bearing checking	--%	$ 52,105	--%	$ 45,308
Savings	0.31	21,491	0.32	19,627
Interest-bearing checking	0.77	294,565	0.78	295,122
Money market	0.93	254,848	0.98	270,942
Total transaction accounts	0.76	623,009	0.80	630,999
Time deposits:				
1.00% to 2.99%		446,297		360,248
3.00% to 4.99%		232,840		197,224
5.00% to 6.99%		21,928		28,292
Total time deposits	2.83	701,065	2.83	585,764
Total deposits	1.85%	$ 1,324,074	1.78%	$ 1,216,763

Note 12 Federal Home Loan Bank Advances and Other Borrowings

At June 30, 2004 and December 31, 2003, the Company was indebted on notes as shown in the following table:

(Dollars in thousands)	June 30, 2004	December 31, 2003
Permanent fixed-rate notes payable to the Federal Home Loan Bank	$ 75,332	$ 125,349
Convertible fixed-rate notes payable to the Federal Home Loan Bank	435,000	435,000
Line of credit with the Federal Home Loan Bank	61,900	71,400
Adjustable-rate note payable to the Federal Home Loan Bank	10,000	10,000

(Dollars in thousands)	June 30, 2004	December 31, 2003
Retail repurchase agreements	6,592	3,947
Junior subordinated debentures	30,928	--
Total Federal Home Loan Bank advances and other borrowings	$ 619,752	$ 645,696

The convertible fixed-rate notes are convertible to adjustable-rate notes at the option of the Federal Home Loan Bank (FHLB), with call dates ranging from August 2004 to January 2008. The line of credit with the FHLB expires in November 2004.

On April 26, 2004, the Company formed a trust (TierOne Capital Trust I) which issued capital securities (Trust Preferred Securities) to investors. The proceeds from the sale of the Trust Preferred Securities were used to purchase junior subordinated debentures issued by the Company. The Company s obligations under the junior subordinated debentures constitute a full and unconditional guarantee by the Company of TierOne Capital Trust s obligations under the Trust Preferred Securities. In accordance with Interpretation No. 46 (Revised), *Consolidation of Variable Interest Entities* (FIN 46R), the trust is not consolidated and related amounts are treated as debt of the Company.

Note 13 Recent Accounting Pronouncements

For discussion regarding accounting pronouncements, interpretations, exposure drafts and other formal accounting guidance and the impact on the Company, reference is made to the Company s Annual Report on Form 10-K for the year ended December 31, 2003. The following discussion identifies accounting guidance issued during 2004.

In March 2004, the FASB issued Staff Accounting Bulletin No. 105 (SAB 105), *Loan Commitments Accounted for as Derivative Instruments*. The requirements of SAB 105 require entities that enter into mortgage loan commitments to disclose their accounting policy for such commitments and include the methods and assumptions used to estimate the fair value of loan commitments in the financial statements. Additionally, any hedging strategy associated with mortgage loan commitments is required to be disclosed. The requirements of SAB 105 must be applied to mortgage loan commitments that are accounted for as derivatives and are entered into after March 31, 2004. SAB 105 permits entities to continue using previously applied accounting policies to loan commitments entered into on or before March 31, 2004. The adoption of SAB 105 did not have a material impact on the Company s consolidated financial statements.

On March 31, 2004, the FASB published an Exposure Draft, *Share-Based Payment, an Amendment of FASB Statements No. 123 and No. 95* (the Exposure Draft). FASB is proposing, among other things, amendments to SFAS No. 123 and thus, the manner in which share-based compensation, such as stock options, will be accounted for by both public and non-public companies. For public companies, the cost of employee services received in exchange for equity instruments including options and restricted stock awards generally would be measured at fair value at the grant date. The grant date fair value would be estimated using option-pricing models adjusted for the unique characteristics of those options and instruments (unless observable market prices for the same or similar options are available). The cost would be recognized over the requisite service period (often the vesting period). The cost of employee services received in exchange for liabilities would be measured initially at the fair value (rather than the previously allowed intrinsic value under APB Opinion No. 25, *Accounting for Stock Issued to Employees*) of the liabilities and would be remeasured subsequently at each reporting date through settlement date.

The proposed changes in accounting would replace existing requirements under SFAS No. 123, *Accounting for Stock-Based Compensation*, and would eliminate the ability to account for share-based compensation transactions using APB Opinion No. 25 which did not require companies to expense options. Under the terms of the Exposure Draft, the accounting for similar transactions involving parties other than employees or the accounting for employee stock ownership plans that are subject to AICPA Statement of Position 93-6, *Employers Accounting for Employee Stock Ownership Plans*, would remain unchanged.

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The Exposure Draft provides that the proposed statement would be applied to public entities prospectively for fiscal years beginning after December 31, 2004, as if all share-based compensation awards vesting, granted, modified, or settled after December 15, 1994 had been accounted for using the fair value-based method of accounting.

The FASB solicited comments on the Exposure Draft through June 30, 2004 and is expected to issue the final statement in the fourth quarter of 2004.

TierOne Corporation and Subsidiaries
Management s Discussion and Analysis of Financial Condition
and Results of Operations

Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations.

General

The Bank, a subsidiary of the Company, is a $2.3 billion federally chartered stock savings bank headquartered in Lincoln, Nebraska. Established in 1907, the Bank offers customers a wide variety of full-service consumer and commercial banking products and services through a geographically diverse network of 57 banking offices located in Nebraska, Iowa and Kansas, three loan production offices located in Colorado and one loan production office located in Minnesota. Product offerings include residential and commercial real estate loans; consumer, construction and business loans; warehouse mortgage lines of credit; consumer and business checking and savings plans; investment and insurance services; and telephone and internet banking.

The Company s results of operations depend, to a large extent, on net interest income, which is the difference between the income earned on its loan and investment securities portfolios and the cost of funds, consisting of the interest paid on deposits and borrowings. Noninterest income, noninterest expense and provisions for loan losses also affect results of operations. Noninterest income consists primarily of fees and service charges related to deposit and lending activities and gains on loans held for sale. Noninterest expense consists of compensation and employee benefits, office occupancy and equipment, data processing, advertising and other operating expense. The Company s results of operations are also significantly affected by general economic and competitive conditions, particularly changes in interest rates, government policies and actions of regulatory authorities. Future changes in applicable law, regulations or government policies may materially impact the Company s financial condition and results of operations.

On March 31, 2004, the Company announced that it had entered into a definitive agreement to acquire United Nebraska Financial Co. (UNFC), the holding company of United Nebraska Bank (UNB) headquartered in Grand Island, Nebraska. The reported assets of UNFC also include an investment in a national bank subsidiary in suburban Phoenix, Arizona, United Arizona Bank (UAB), which will be sold prior to the completion of the transaction. The Company will pay $97.3 million in cash, subject to a post-closing adjustment, to acquire UNFC. The purchase price represents approximately 1.9 times UNFC s December 31, 2003 stated book value of $51.8 million. At December 31, 2003, UNB operated from 16 banking offices located in Broken Bow, Burwell, Callaway, Columbus, Grand Island, Holdrege, Lexington, North Platte, Omaha, O Neill and Ord, Nebraska. At March 31, 2004, UNB had total assets of $506.3 million. The Company received regulatory approvals to acquire UNFC on July 26, 2004 with closing anticipated in the third quarter of 2004.

As used in this report, unless the context otherwise requires, the terms we, us, or our refer to TierOne Corporation, a Wisconsin corporation, and our wholly owned subsidiary, TierOne Bank, a federally chartered stock savings bank.

Forward-Looking Statements

Statements contained in this quarterly report on Form 10-Q which are not historical facts may be forward-looking statements as that term is defined in the Private Securities Litigation Reform Act of 1995. Such forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those currently anticipated due to a number of factors. Factors which could result in material variations include, but are not limited to, changes in interest rates which could affect net interest margins and net interest income; competitive factors which could affect net interest income and noninterest income; changes in demand for loans, deposits and other financial services in the Company s market area; unanticipated issues that could negatively impact the historic redeposit rate of maturing time deposits; changes in asset quality and general economic conditions; unanticipated issues associated with the execution of the Company s strategic plan; unanticipated difficulties in realizing the growth opportunities and cost savings from the acquisition of UNFC, unanticipated issues related to the completion of the acquisition and the resultant integration of UNFC. and UNB; as well as other factors discussed in documents filed by the Company with the Securities and Exchange Commission from time to time. These factors should be considered in evaluating the forward-looking statements and undue reliance should not be placed on such statements. The Company assumes no obligation, and disclaims any obligation, to update information contained in this quarterly report on Form 10-Q, including forward-looking statements, to reflect events or circumstances that occur after the date on which such statements were made.

Critical Accounting Policies

Allowance for Loan Losses

We have identified the evaluation of the allowance for loan losses as a critical accounting policy where amounts are sensitive to material variation. This policy is significantly affected by our judgment and uncertainties and there is a likelihood that materially different amounts would be reported under different, but reasonably plausible, conditions or assumptions. The allowance for loan losses is considered a critical accounting estimate because there is a large degree of judgment in:

- Assigning individual loans to specific risk levels (pass, special mention, substandard, doubtful and loss);
- Valuing the underlying collateral securing the loans;
- Determining the appropriate reserve factor to be applied to specific risk levels for special mention loans and those adversely classified (substandard, doubtful and loss); and

- Determining reserve factors to be applied to pass loans based upon loan type.

We establish provisions for loan losses, which are charges to our operating results, in order to maintain a level of total allowance for loan losses that management believes covers all known and inherent losses that are both probable and reasonably estimable at each reporting date. Management reviews the loan portfolio no less frequently than quarterly in order to identify those inherent losses and to assess the overall collection probability of the loan portfolio. Management s review includes a quantitative analysis by loan category, using historical loss experience, classifying loans pursuant to a grading system and consideration of a series of qualitative loss factors. The evaluation process includes, among other things:

- An analysis of delinquency trends;
- Nonperforming loan trends;
- Levels of charge-offs and recoveries;
- Prior loss experience;
- Total loans outstanding;
- Volume of loan originations;
- Type, size, terms and geographic concentration of loans held by us;