

TIERONE CORP
Form 10-Q
November 10, 2008

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

FORM 10-Q

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

FOR THE QUARTERLY PERIOD ENDED SEPTEMBER 30, 2008

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 No

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 definitions of large accelerated filer, accelerated filer, and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

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

Indicated by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of November 7, 2008 there were 18,035,192 issued and outstanding shares of the Registrant's common stock.

FOR THE TRANSITION PERIOD FROM ____ TO ____.

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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. In addition to the risk factors described in Part 2, Item 1A. of this Quarterly Report on Form 10-Q, factors that could result in material variations include, but are not limited to:

- General economic conditions and trends, either nationally or in some or all of the areas in which we and our customers conduct our businesses;
- Changes in interest rates or other competitive factors which could affect net interest margins, net interest income and noninterest income;
- Changes in deposit flows, and in the demand for deposits, loans, investment products and other financial services in the markets we serve;
- Changes in the quality or composition of our loan portfolio, or the unanticipated deterioration of our loan portfolio;
- Changes in our underlying assumptions or any unanticipated issues that could impact management's judgment regarding our allowance and provisions for loan losses;
- Changes in real estate values, which could impact the quality of the assets securing the loans in our portfolios;
- Changes in the financial or operating performance of our customers' businesses;
- Unanticipated issues associated with increases in the levels of losses, customer bankruptcies, claims and assessments;
- Our timely development of new lines of business and competitive products or services within our existing lines of business in a changing environment, and the acceptance of such products and services by our customers;
- Any interruption or breach of security resulting in failures or disruption in customer account management, general ledger, deposit operations, lending or other systems;

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Changes in fiscal, monetary, regulatory, trade and tax policies and laws;
 Increased competitive challenges and expanding product and pricing pressures among financial institutions;
 Changes in accounting policies or procedures as may be required by various regulatory agencies;
 Changes in consumer spending and savings habits;
 Unanticipated issues relating to the recovery of insurance proceeds for claims arising out of our prior relationship with TransLand Financial Services, Inc.;

Unanticipated issues related to our ability to achieve expected results pursuant to our plan to address asset quality, restore long-term profitability and increase capital;
 Actions by federal and state agencies;
 Changes in liquidity levels in capital markets; and
 Other factors discussed in documents we may file 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. We undertake no obligation, and disclaim any obligation, to update information contained in this Quarterly Report on Form 10-Q, including these forward-looking statements, to reflect events or circumstances that occur after the date of the filing of this Quarterly Report on Form 10-Q.

Item 1 Financial Statements

TierOne Corporation and Subsidiaries Consolidated Statements of Financial Condition September 30, 2008 (Unaudited) and December 31, 2007

(Dollars in thousands, except per share data)

	September 30, 2008	December 31, 2007
ASSETS		
Cash and due from banks	\$ 74,726	\$ 79,561
Federal funds sold	49,000	161,900
Total cash and cash equivalents	123,726	241,461
Investment securities:		
Held to maturity, at cost which approximates fair value	54	70
Available for sale, at fair value	163,111	130,481
Mortgage-backed securities, available for sale, at fair value	3,615	6,689
Loans receivable:		
Net loans (includes loans held for sale of \$11,532 and \$9,348 at September 30, 2008 and December 31, 2007, respectively)	2,777,706	2,976,129
Allowance for loan losses	(62,964)	(66,540)
Net loans after allowance for loan losses	2,714,742	2,909,589
FHLBank Topeka stock, at cost	46,739	65,837
Premises and equipment, net	36,312	38,028
Accrued interest receivable	18,423	21,248
Goodwill	--	42,101
Other intangible assets, net	5,044	6,744
Mortgage servicing rights, net	16,148	14,530
Other assets	88,833	60,988
Total assets	\$ 3,216,747	\$ 3,537,766
LIABILITIES AND STOCKHOLDERS EQUITY		
Liabilities:		
Deposits	\$ 2,206,819	\$ 2,430,544

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(Dollars in thousands, except per share data)

September 30, 2008

December 31, 2007

FHLBank Topeka advances and other borrowings	677,382	689,288
Advance payments from borrowers for taxes, insurance and other escrow funds	24,843	30,205
Accrued interest payable	4,442	6,269
Accrued expenses and other liabilities	29,524	35,870
Total liabilities	2,943,010	3,192,176
Stockholders 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; 18,036,134 and 18,058,946 shares issued at September 30, 2008 and December 31, 2007, respectively	226	226
Additional paid-in capital	367,235	366,042
Retained earnings, substantially restricted	21,117	94,630
Treasury stock, at cost; 4,538,941 and 4,516,129 shares at September 30, 2008 and December 31, 2007, respectively	(105,201)	(105,008)
Unallocated common stock held by Employee Stock Ownership Plan	(9,030)	(10,159)
Accumulated other comprehensive loss, net	(610)	(141)
Total stockholders equity	273,737	345,590
Total liabilities and stockholders equity	\$ 3,216,747	\$ 3,537,766

See accompanying notes to consolidated financial statements.

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**TierOne Corporation and Subsidiaries
Consolidated Statements of Operations
(Unaudited)**

**For the Three Months Ended
September 30,**

**For the Nine Months Ended
September 30,**

(Dollars in thousands, except per share data)

	2008		2007	
Interest income:				
Loans receivable	\$ 41,659	\$ 55,969	\$ 132,979	\$ 168,505
Investment securities	1,636	2,993	5,515	8,277
Other interest-earning assets	461	943	2,418	1,329
Total interest income	43,756	59,905	140,912	178,111
Interest expense:				
Deposits	14,450	21,828	50,865	59,087
FHLBank Topeka advances and other borrowings	7,434	8,761	22,243	27,829
Total interest expense	21,884	30,589	73,108	86,916
Net interest income	21,872	29,316	67,804	91,195
Provision for loan losses	5,973	17,483	73,607	29,184

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	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
Net interest income (loss) after provision for loan losses	15,899	11,833	(5,803)	62,011
Noninterest income:				
Fees and service charges	6,516	6,050	18,362	17,249
Debit card fees	1,050	871	3,039	2,492
Loss from real estate operations, net	(227)	(191)	(459)	(470)
Loss on impairment of securities	(355)	--	(949)	--
Net gain (loss) on sales of:				
Loans held for sale	223	374	1,606	1,936
Real estate owned	(66)	147	(88)	(185)
Other operating income	1,778	273	2,664	830
Total noninterest income	8,919	7,524	24,175	21,852
Noninterest expense:				
Salaries and employee benefits	11,382	13,010	36,014	39,306
Goodwill impairment	--	--	42,101	--
Occupancy, net	2,594	2,409	7,474	7,213
Data processing	497	610	1,764	1,807
Advertising	977	1,525	3,015	3,790
Other operating expense	6,073	10,108	17,810	19,858
Total noninterest expense	21,523	27,662	108,178	71,974
Income (loss) before income taxes	3,295	(8,305)	(89,806)	11,889
Income tax expense (benefit)	1,156	(2,425)	(18,317)	5,932
Net income (loss)	\$ 2,139	\$ (5,880)	\$ (71,489)	\$ 5,957
Net income (loss) per common share, basic	\$ 0.13	\$ (0.35)	\$ (4.24)	\$ 0.36
Net income (loss) per common share, diluted	\$ 0.13	\$ (0.35)	\$ (4.24)	\$ 0.35
Dividends declared per common share	\$ --	\$ 0.08	\$ 0.12	\$ 0.23
Average common shares outstanding, basic (000 s)	16,855	16,758	16,875	16,679
Average common shares outstanding, diluted (000 s)	16,855	16,758	16,875	17,178

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Changes in Stockholders Equity and Comprehensive Income
For the Nine Months Ended September 30, 2008 and 2007
(Unaudited)

<i>(Dollars in thousands)</i>	Common Stock	Additional Paid-In Capital	Retained Earnings, Substantially Restricted	Treasury Stock	Unallocated Common Stock Held by the Employee Stock Ownership Plan	Accumulated Other Comprehensive Loss, Net	Total Stockholders Equity
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Balance at December 31, 2006	\$	226	\$ 358,733	\$	112,111	\$ (105,406)	\$	(11,664)	\$	(717)	\$	353,283
Common stock earned by employees in Employee Stock Ownership Plan	--		1,951	--		--		1,129	--			3,080
Amortization of awards under the Management Recognition and Retention Plan	--		2,178	--		--		--	--			2,178
Amortization of stock options under 2003 Stock Option Plan	--		1,261	--		--		--	--			1,261
Repurchase of common stock (7,111 shares)	--		--	--		(175)		--	--			(175)
Treasury stock reissued under 2003 Stock Option Plan	--		(108)	--		463		--	--			355
Excess tax benefit realized from stock-based compensation plans	--		423	--		--		--	--			423
Dividends paid (\$0.23 per common share)	--		--		(3,861)	--		--	--			(3,861)
Cumulative effect of adoption of FASB Interpretation No. 48 on January 1, 2007	--		--		157	--		--	--			157
Comprehensive income:												
Net income	--		--		5,957	--		--	--			5,957
Change in unrealized loss on available for sale securities, net of tax and reclassification adjustment	--		--		--	--		--		419		419
Total comprehensive income	--		--		5,957	--		--		419		6,376
Balance at September 30, 2007	\$	226	\$ 364,438	\$	114,364	\$ (105,118)	\$	(10,535)	\$	(298)	\$	363,077
Balance at December 31, 2007	\$	226	\$ 366,042	\$	94,630	\$ (105,008)	\$	(10,159)	\$	(141)	\$	345,590
Common stock earned by employees in Employee Stock Ownership Plan	--		(27)	--		--		1,129	--			1,102
Amortization of awards under the Management Recognition and Retention Plan	--		1,001	--		--		--	--			1,001
Amortization of stock options under 2003 Stock Option Plan	--		683	--		--		--	--			683
Repurchase of common stock (23,812 shares)	--		--	--		(216)		--	--			(216)
Treasury stock reissued under 2003 Stock Option Plan	--		(5)	--		23		--	--			18
Excess tax expense realized from stock-based compensation plans	--		(459)	--		--		--	--			(459)
Dividends paid (\$0.12 per common share)	--		--		(2,024)	--		--	--			(2,024)
Comprehensive loss:												
Net loss	--		--		(71,489)	--		--	--			(71,489)
Change in unrealized loss on available for sale securities, net of tax	--		--		--	--		--		(469)		(469)
Total comprehensive loss	--		--		(71,489)	--		--		(469)		(71,958)
Balance at September 30, 2008	\$	226	\$ 367,235	\$	21,117	\$ (105,201)	\$	(9,030)	\$	(610)	\$	273,737

See accompanying notes to consolidated financial statements.

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TierOne Corporation and Subsidiaries
Consolidated Statements of Cash Flows (continued) (Unaudited)

For the Nine Months Ended
September 30,

(Dollars in thousands)

	2008	2007
Cash flows from operating activities:		
Net income (loss)	\$ (71,489)	\$ 5,957
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Net discount accretion of investment and mortgage-backed securities	(1,889)	(1,073)
Premises and equipment depreciation and amortization	3,051	3,016
Amortization of other intangible assets	1,157	1,257
Accretion of discount on FHLBank Topeka advances	(191)	(191)
Employee Stock Ownership Plan compensation expense	1,102	3,080
2003 Management Recognition and Retention Plan compensation expense	1,001	2,178
2003 Stock Option Plan compensation expense	683	1,261
Net accretion of discounts on net loans	(232)	(2,781)
FHLBank Topeka stock dividend	(1,902)	(2,914)
Deferred income tax expense (benefit)	1,235	(11,780)
Goodwill impairment	42,101	--
Impairment of investment securities	949	--
Provision for loan losses	73,607	29,184
Provision for real estate owned losses	1,093	177
Provision for uncollectible receivable	-	4,767
Mortgage servicing rights originated, net	(1,694)	(1,229)
Mortgage servicing rights valuation allowance	76	--
Proceeds from sales of loans held for sale	299,607	235,307
Originations and purchases of loans held for sale	(300,185)	(234,548)
Excess tax expense (benefit) from stock-based compensation plans	459	(423)
Net (gain) loss on sales of:		
Loans held for sale	(1,606)	(1,936)
Real estate owned	88	185
Premises and equipment	2	9
Changes in certain assets and liabilities:		
Accrued interest receivable	2,825	(832)
Other assets	(19,892)	(19,749)
Accrued interest payable	(1,827)	(488)
Accrued expenses and other liabilities	(2,769)	5,456
Net cash provided by operating activities	25,360	13,890
Cash flows from investing activities:		
Purchase of investment and mortgage-backed securities, available for sale	(363,918)	(230,338)
Proceeds from sale of investment and mortgage-backed securities, available for sale	--	10
Proceeds from maturities of investment securities, available for sale	331,484	187,281
Proceeds from principal repayments of investment and mortgage-backed securities, available for sale and held to maturity	3,110	4,651
Decrease in loans receivable	104,567	24,076
Sale of FHLBank Topeka stock	21,000	--
Additions to premises and equipment	(1,340)	(1,729)
Proceeds from sale of premises and equipment	3	--
Proceeds from sale of real estate owned	5,482	3,647
Net cash provided by (used in) investing activities	100,388	(12,402)

See accompanying notes to consolidated financial statements.

TierOne Corporation and Subsidiaries
Consolidated Statements of Cash Flows (continued) (Unaudited)

<i>(Dollars in thousands)</i>	For the Nine Months Ended September 30,	
	2008	2007
Cash flows from financing activities:		
Net increase (decrease) in deposits	\$ (223,725)	\$ 302,495
Net advances (repayment) on FHLBank Topeka line of credit, short-term advances and other borrowings	13,453	(44,722)
Proceeds from FHLBank Topeka long-term advances and other borrowings	--	50,000
Repayments of FHLBank Topeka long-term advances and other borrowings	(25,168)	(200,160)
Net increase in advances from borrowers for taxes, insurance and other escrow funds	(5,362)	(10,096)
Repurchase of common stock	(216)	(175)
Dividends paid on common stock	(2,024)	(3,861)
Excess tax benefit realized from the exercise of stock options	--	45
Excess tax benefit (expense) realized from the vesting of Management Recognition and Retention Plan shares	(459)	378
Proceeds from the exercise of stock options	18	355
<hr/>		
Net cash provided by (used in) financing activities	(243,483)	94,259
<hr/>		
Net increase (decrease) in cash and cash equivalents	(117,735)	95,747
Cash and cash equivalents at beginning of period	241,461	86,808
<hr/>		
Cash and cash equivalents at end of period	\$ 123,726	\$ 182,555
<hr/>		
Supplemental disclosures of cash flow information:		
Cash paid during period for:		
Interest	\$ 74,935	\$ 87,404
Income taxes, net of refunds	\$ --	\$ 17,265
<hr/>		
Noncash investing activities:		
Transfers from loans to real estate owned and other assets through foreclosure	\$ 19,089	\$ 5,657

See accompanying notes to consolidated financial statements.

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

Note 1 Basis of Presentation and Consolidation

TierOne Corporation (Company) is a Wisconsin corporation headquartered in Lincoln, Nebraska. TierOne Corporation is the holding company for TierOne Bank (Bank). The Bank has two wholly owned subsidiaries, TMS Corporation of the Americas (TMS) and United Farm &

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Ranch Management, Inc. (UFARM). TMS is the holding company of TierOne Investments and Insurance, Inc. (d/b/a TierOne Financial), a wholly owned subsidiary that administers the sale of securities and insurance products, and TierOne Reinsurance Company, a wholly owned subsidiary that reinsures credit life and disability insurance policies. UFARM provides agricultural customers with professional farm and ranch management and real estate brokerage services. The accompanying unaudited consolidated financial statements include the accounts of the Bank and its wholly owned subsidiaries.

The assets of the Company, on an unconsolidated basis, primarily consist of 100% of the Bank's common stock. The Company has no significant independent source of income and therefore depends on cash distributions from the Bank to meet its funding requirements.

The accompanying interim consolidated financial statements as of September 30, 2008 and for the three and nine months ended September 30, 2008 and 2007 are unaudited. 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 of the financial position and operating results for interim periods. The unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information, in accordance with instructions to Form 10-Q and Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission (SEC), and do not include all of the information and notes required for complete, audited financial statements. The unaudited consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2007. The results of operations for the three and nine months ended September 30, 2008 are not necessarily indicative of the results which may be expected for the entire calendar year 2008.

As used in this report, unless the context otherwise requires, the terms we, us, or our refer to the Company and the Bank.

Note 2 Termination of Acquisition Agreement

On May 17, 2007, the Company, CapitalSource Inc. and CapitalSource TRS Inc. entered into an Agreement and Plan of Merger (Merger Agreement). On March 20, 2008, the Company terminated the Merger Agreement. Pursuant to the terms of the Merger Agreement, either party had the right to terminate the Merger Agreement if the proposed merger was not completed by February 17, 2008. No termination fee was payable by either company as a result of the termination of the Merger Agreement.

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

Note 3 Earnings Per Share

Basic earnings (loss) per share (EPS) is computed by dividing net income (loss) by the weighted average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised. Diluted earnings per share is computed after giving consideration to the weighted average dilutive effect of our 2003 Stock Option Plan shares and 2003 Management Recognition and Retention Plan shares. All stock options are assumed to be 100% vested for purposes of EPS computations. Due to our net loss for the nine months ended September 30, 2008, no potentially dilutive shares were included in the loss per share calculation for the nine months ended September 30, 2008 as including such shares would be anti-dilutive. The following table is a reconciliation of basic and diluted EPS:

<i>(In thousands, except per share data)</i>	For the Three Months Ended September 30,			
	2008		2007	
	Basic EPS	Diluted EPS	Basic EPS	Diluted EPS
Net income (loss)	\$ 2,139	\$ 2,139	\$ (5,880)	\$ (5,880)
Total weighted average basic common shares outstanding	16,855	16,855	16,758	16,758
Effect of dilutive securities:				
2003 Stock Option Plan		--		--
2003 Management Recognition and Retention Plan		--		--

For the Three Months Ended September 30,

Total weighted average basic and diluted common shares outstanding	16,855	16,855	16,758	16,758
Net income (loss) per common share	\$ 0.13	\$ 0.13	\$ (0.35)	\$ (0.35)

For the Nine Months Ended September 30,

	2008		2007	
	Basic EPS	Diluted EPS	Basic EPS	Diluted EPS
<i>(In thousands, except per share data)</i>				
Net income (loss)	\$ (71,489)	\$ (71,489)	\$ 5,957	\$ 5,957
Total weighted average basic common shares outstanding	16,875	16,875	16,679	16,679
Effect of dilutive securities:				
2003 Stock Option Plan		--		468
2003 Management Recognition and Retention Plan		--		31
Total weighted average basic and diluted common shares outstanding	16,875	16,875	16,679	17,178
Net income (loss) per common share	\$ (4.24)	\$ (4.24)	\$ 0.36	\$ 0.35

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

Note 4 Investment and Mortgage-Backed Securities

Investment Security Composition. The amortized cost, gross unrealized gains and losses and fair value of investment and mortgage-backed securities by major security category at September 30, 2008 and December 31, 2007 are as follows:

	September 30, 2008			
	Amortized Cost	Gross Unrealized		Fair Value
Gains		Losses		
<i>(Dollars in thousands)</i>				
Held to maturity:				
Municipal obligations	\$ 54	\$ --	\$ --	\$ 54
Available for sale:				
Mortgage-backed securities	3,628	42	55	3,615
U.S. Government securities and agency obligations	142,602	30	38	142,594
Corporate securities	4,054	--	449	3,605
Municipal obligations	11,995	25	37	11,983
Agency equity securities	23	--	--	23

	September 30, 2008			
Asset Management Fund - ARM Fund	5,377	--	471	4,906
Total investment and mortgage-backed securities, available for sale	\$ 167,679	\$ 97	\$ 1,050	\$ 166,726
	December 31, 2007			
	Gross Unrealized			
<i>(Dollars in thousands)</i>	Amortized Cost	Gains	Losses	Fair Value
Held to maturity:				
Municipal obligations	\$ 70	\$ --	\$ --	\$ 70
Available for sale:				
Mortgage-backed securities	6,755	32	98	6,689
U.S. Government securities and agency obligations	105,428	18	33	105,413
Corporate securities	4,935	--	15	4,920
Municipal obligations	13,931	18	35	13,914
Agency equity securities	536	--	114	422
Asset Management Fund - ARM Fund	5,812	--	--	5,812
Total investment and mortgage-backed securities, available for sale	\$ 137,397	\$ 68	\$ 295	\$ 137,170

We believe all unrealized losses as of September 30, 2008 to be market related, with no permanent sector or issuer credit concerns or impairments. We had seven securities with unrealized losses totaling \$76,000 for 12 consecutive months or longer as of September 30, 2008. The unrealized losses are believed to be temporary. Impairment is deemed temporary if the positive evidence indicating that an investment's carrying amount is recoverable within a reasonable time period outweighs negative evidence to the contrary. At September 30, 2008, we have the ability and intent to hold these securities until maturity.

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

Note 5 Loans Receivable

Loan Portfolio Composition. Loans receivable at September 30, 2008 and December 31, 2007 are summarized in the following table:

	September 30, 2008		December 31, 2007	
<i>(Dollars in thousands)</i>	Amount	%	Amount	%
Real estate loans:				
One-to-four family residential (1)	\$ 364,989	12.30 %	\$ 314,623	9.41 %
Second mortgage residential	80,182	2.70	95,477	2.86
Multi-family residential	181,613	6.12	106,678	3.19
Commercial real estate	335,668	11.31	370,910	11.10
Land and land development	419,070	14.12	473,346	14.16
Residential construction	269,097	9.06	513,560	15.36
Commercial construction	424,898	14.31	540,797	16.18
Agriculture	100,533	3.39	91,068	2.72

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	<u>September 30, 2008</u>		<u>December 31, 2007</u>	
Total real estate loans	2,176,050	73.31	2,506,459	74.98
Business	234,151	7.89	252,712	7.56
Agriculture - operating	106,980	3.60	100,365	3.00
Warehouse mortgage lines of credit	72,583	2.45	86,081	2.58
Consumer loans:				
Home equity	58,649	1.98	72,517	2.17
Home equity lines of credit	123,734	4.17	120,465	3.60
Home improvement	39,057	1.31	46,045	1.38
Automobile	88,106	2.97	87,079	2.60
Other	69,022	2.32	71,141	2.13
Total consumer loans	378,568	12.75	397,247	11.88
Total loans	2,968,332	100.00 %	3,342,864	100.00 %
Unamortized premiums, discounts and deferred loan fees	9,526		9,451	
Loans in process (2)	(200,152)		(376,186)	
Net loans	2,777,706		2,976,129	
Allowance for loan losses	(62,964)		(66,540)	
Net loans after allowance for loan losses	\$ 2,714,742		\$ 2,909,589	
(1) Includes loans held for sale	\$ 11,532		\$ 9,348	

(2) Loans in process represents the undisbursed portion of construction and land development loans.

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Impaired Loans. Information about our impaired loans and the allowance for loan losses related to impaired loans is as follows:

<i>(Dollars in thousands)</i>	September 30, 2008		December 31, 2007	
Impaired loans (1)	\$	158,136	\$	125,946
Allowance for loan losses related to impaired loans (2)		13,035		24,640

(1) Impaired loans are performing and nonperforming loans which management believes it will not collect all principal and interest due under the original loan terms.

(2) Allowance for loan losses related to impaired loans is included in the total allowance for loan losses of \$63.0 million and \$66.5 million at September 30, 2008 and December 31, 2007, respectively.

The decrease in our allowance for loan losses related to impaired loans was primarily attributable to charge-offs during the nine months ended September 30, 2008.

Note 6 Goodwill and Other Intangible Assets

Goodwill. We recorded goodwill as a result of our 2004 acquisition of United Nebraska Financial Co. (UNFC). In accordance with Statement of Financial Accounting Standard (SFAS) No. 142, *Goodwill and Other Intangible Assets*, we tested this goodwill for impairment annually during the third quarter of each year, or between annual assessment dates whenever events or significant changes in circumstances indicate that the carrying value may be impaired. We performed a goodwill impairment test as of March 31, 2008 due to adverse changes in the business climate. As a result of a decline in the market value of our common stock to levels below our book value, we determined that the entire amount of our goodwill was impaired, and we recorded a \$42.1 million goodwill impairment charge to write-off our goodwill at March 31, 2008. The changes in the carrying amount of goodwill for the three and nine months ended September 30, 2008 and 2007 are as follows:

<i>(Dollars in thousands)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Balance at beginning of period	\$ --	\$ 42,162	\$ 42,101	\$ 42,228
Adjustment due to adoption of FASB Interpretation No. 48	--	--	--	(66)
Realized tax benefit associated with United Nebraska Financial Co. acquisition	--	(61)	--	(61)
Goodwill impairment	--	--	(42,101)	--
Balance at end of period	\$ --	\$ 42,101	\$ --	\$ 42,101

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Other Intangible Assets. Our only identifiable other intangible asset is the value of core deposits acquired as part of the UNFC and Marine Bank transactions. The core deposit intangible assets have been estimated to have nine- to ten-year lives. Core deposit intangible assets are amortized using an accelerated method of amortization which is recorded in other operating expense.

Other Intangible Asset Activity. The changes in the carrying amount of acquired intangible assets for the three and nine months ended September 30, 2008 and 2007 are as follows:

<i>(Dollars in thousands)</i>	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
Balance at beginning of period	\$ 5,964	\$ 7,544	\$ 6,744	\$ 8,391
Realized tax benefit associated with United Nebraska Financial Co. acquisition	(543)	--	(543)	--
Amortization expense	(377)	(410)	(1,157)	(1,257)
Balance at end of period	\$ 5,044	\$ 7,134	\$ 5,044	\$ 7,134

Other Intangible Asset Estimated Amortization. Estimated amortization expense related to our core deposit intangible assets for the year ending December 31, 2008 and the five years thereafter are as follows:

(Dollars in thousands)

Estimated Amortization Expense For the Year Ending:

December 31, 2008	\$ 1,513
December 31, 2009	1,373
December 31, 2010	1,222

(Dollars in thousands)

December 31, 2011	1,052
December 31, 2012	850
December 31, 2013	553

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TierOne Corporation and Subsidiaries
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Note 7 Mortgage Servicing Rights

On January 1, 2007, we adopted SFAS No. 156, *Accounting for Servicing of Financial Assets – an Amendment of FASB Statement No. 140* (SFAS No. 156). In accordance with SFAS No. 156, we utilize the amortization method for all of our mortgage servicing right assets, thus, carrying our mortgage servicing rights at the lower of cost or market (fair value). Under the amortization method, we amortize mortgage servicing rights in proportion to and over the period of net servicing income. Income generated as a result of newly acquired servicing assets is reported as net gain on sale of loans in the Consolidated Statements of Operations. Loan servicing fees, net of amortization of mortgage servicing rights, are recorded in fees and service charges in the Consolidated Statements of Operations.

We primarily service one-to-four family residential mortgage loans. We obtain mortgage servicing right assets when we deliver loans, both originated and purchased, as an agent into the secondary market on a servicing-retained basis. Initial fair value of the servicing right is calculated by a discounted cash flow model based on market value assumptions at the time of origination.

The balance of capitalized mortgage servicing rights, net of valuation allowances, at September 30, 2008 and December 31, 2007 was \$16.1 million and \$14.5 million, respectively. The following are the key assumptions used in measuring the fair values of capitalized mortgage servicing rights and the sensitivity of the fair values to changes in those assumptions:

<i>(Dollars in thousands)</i>	September 30, 2008	December 31, 2007
Serviced loan portfolio balance	\$1,590,004	\$1,459,498
Fair value	\$17,936	\$18,310
Prepayment speed	4.74% - 47.16%	6.62% - 26.07%
Weighted average prepayment speed	10.90%	10.37%
Fair value with 10% adverse change	\$17,350	\$17,860
Fair value with 20% adverse change	\$16,744	\$17,166
Discount rate	11.00% - 14.00%	9.50% - 13.00%
Weighted average discount rate	11.94%	10.63%
Fair value with 10% adverse change	\$17,205	\$17,866
Fair value with 20% adverse change	\$16,477	\$17,178

The sensitivity of the fair values is hypothetical and should be used with caution. As the figures indicate, changes in fair value based on a variation in assumptions generally cannot be extrapolated because the relationship of the change in assumptions to the change in fair value may not be linear. Also, in the table, the effect of a variation in a particular assumption on the fair value of the mortgage servicing rights is calculated without changing any other assumption. In reality, changes in one assumption may result in changes in another that might magnify or counteract the sensitivities.

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Mortgage Servicing Rights Activity. The following table summarizes mortgage servicing rights activity including amortization expense:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<i>(Dollars in thousands)</i>				
Balance at beginning of period	\$ 16,211	\$ 12,930	\$ 14,530	\$ 12,467
Mortgage servicing rights capitalized	871	1,533	4,885	3,530
Amortization expense	(869)	(767)	(3,191)	(2,301)
Valuation adjustment	(65)	--	(76)	--
Balance at end of period	\$ 16,148	\$ 13,696	\$ 16,148	\$ 13,696

Mortgage Servicing Rights Valuation Allowance. The valuation allowance on mortgage servicing rights is summarized in the following table for the periods presented:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<i>(Dollars in thousands)</i>				
Balance at beginning of period	\$ (11)	\$ --	\$ --	\$ --
Changes in mortgage servicing valuation reserve	(65)	--	(76)	--
Balance at end of period	\$ (76)	\$ --	\$ (76)	\$ --

We evaluate the fair value of mortgage servicing rights on a quarterly basis using current prepayment speeds, cash flow and discount rate estimates. Changes in these estimates impact fair value and could require us to record a valuation allowance or recovery. The amortization expense and valuation adjustment are recorded as a reduction of fees and service charges in the accompanying Consolidated Statements of Operations.

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Note 8 Deposits

Deposit Composition. Deposits at September 30, 2008 and December 31, 2007 are summarized in the following table:

	September 30, 2008		December 31, 2007	
	Weighted Average Rates	Amount	Weighted Average Rates	Amount
<i>(Dollars in thousands)</i>				
Transaction accounts:				
Noninterest-bearing checking	-- %	\$ 157,292	-- %	\$ 164,275
Savings	2.00	206,812	3.55	188,613
Interest-bearing checking	0.77	311,151	1.12	328,267

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	September 30, 2008		December 31, 2007	
Money market	1.31	264,995	2.81	350,276
Total transaction accounts	1.06	940,250	1.96	1,031,431
Total transaction accounts as a percentage of total deposits		42.61 %		42.44 %
Time deposits:				
0.00% to 0.99%		34		20
1.00% to 1.99%		395		101
2.00% to 2.99%		340,489		3,879
3.00% to 3.99%		621,414		129,910
4.00% to 4.99%		275,597		398,325
5.00% to 5.99%		28,640		866,878
Total time deposits	3.59	1,266,569	4.96	1,399,113
Total time deposits as a percentage of total deposits		57.39 %		57.56 %
Total deposits	2.51 %	\$ 2,206,819	3.69 %	\$ 2,430,544

Time Deposit Maturity. The scheduled maturities of time deposits at September 30, 2008 are presented in the following table:

<i>(Dollars in thousands)</i>	Amount	Percent
Amount Maturing During the 12 Months Ending:		
September 30, 2009	\$ 1,009,547	79.71 %
September 30, 2010	234,011	18.48
September 30, 2011	9,822	0.78
September 30, 2012	5,508	0.43
September 30, 2013	7,567	0.59
Thereafter	114	0.01
Total time deposits	\$ 1,266,569	100.00 %

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Time Deposits of \$100,000 or More. The following table shows the maturities of our time deposits of \$100,000 or more at September 30, 2008 by the time remaining to maturity.

<i>(Dollars in thousands)</i>	Amount	Weighted Average Rate
Amount Maturing During the Quarter Ended:		
December 31, 2008	\$ 74,776	4.31 %
March 31, 2009	75,475	3.14
June 30, 2009	36,936	3.65

<i>(Dollars in thousands)</i>	Amount	Weighted Average Rate
September 30, 2009	65,034	3.66
Thereafter	56,107	3.89
Total time deposits of \$100,000 or more	\$ 308,328	3.73 %

Time Deposits of \$250,000 or More. The *Emergency Economic Stabilization Act of 2008* included a provision that temporarily raises the Federal Deposit Insurance Corporation (FDIC) insurance coverage limit on non-retirement accounts from \$100,000 to \$250,000 per account holder per institution. This increase in the insurance coverage limit is effective until December 31, 2009. The following table shows the maturities of our time deposits of \$250,000 or more at September 30, 2008 by the time remaining to maturity.

<i>(Dollars in thousands)</i>	Amount	Weighted Average Rate
Amount Maturing During the Quarter Ended:		
December 31, 2008	\$ 18,854	4.55 %
March 31, 2009	19,573	3.05
June 30, 2009	10,272	3.93
September 30, 2009	5,703	3.71
Thereafter	10,085	4.14
Total time deposits of \$250,000 or more	\$ 64,487	3.86 %

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Note 9 FHLBank Topeka Advances and Other Borrowings

At September 30, 2008 and December 31, 2007, we were indebted on notes as shown in the following table:

<i>(Dollars in thousands)</i>	September 30, 2008	December 31, 2007
Permanent fixed-rate notes payable to the FHLBank Topeka	\$ 8,836	\$ 9,195
Convertible fixed-rate notes payable to the FHLBank Topeka	600,000	625,000
Retail repurchase agreements	37,618	24,165
Junior subordinated debentures	30,928	30,928
Total FHLBank Topeka advances and other borrowings	\$ 677,382	\$ 689,288
Weighted average interest rate	4.34%	4.50%

The convertible fixed-rate notes are convertible to adjustable-rate notes at the option of the FHLBank Topeka (FHLBank). We did not have an outstanding balance on our FHLBank line of credit at both September 30, 2008 and December 31, 2007. The line of credit with the FHLBank expires in November 2008. We expect the line of credit agreement to be renewed in the ordinary course of business.

Pursuant to our collateral agreement with the FHLBank, such advances are secured by our qualifying residential, multi-family residential and commercial real estate mortgages, residential construction, commercial construction and agricultural real estate loans. Under our collateral agreement with the FHLBank, our borrowing capacity at September 30, 2008 was \$742.2 million. Other qualifying collateral can be pledged in the event additional borrowing capacity is required.

Our retail repurchase agreements are primarily collateralized by governmental agency and municipal obligations (investment securities).

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Note 10 Stock-Based Benefit Plans

General. We account for our stock-based benefit plans using SFAS No. 123(R), *Share-Based Payment* (SFAS No. 123(R)). SFAS No. 123(R) requires that compensation expense related to stock-based payment transactions be recognized in the financial statements and that expense be measured based on the fair value of the equity or liability instrument issued. SFAS No. 123(R) also requires that forfeitures be estimated over the vesting period of the instrument.

Stock-Based Employee Compensation Expense. Amounts recognized in the financial statements with respect to our Employee Stock Ownership Plan (ESOP) and stock-based employee compensation plans are presented in the following table:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<i>(Dollars in thousands)</i>				
Stock-based employee compensation expense:				
Employee Stock Ownership Plan	\$ 164	\$ 885	\$ 1,012	\$ 2,940
Management Recognition and Retention Plan	47	726	1,001	2,178
2003 Stock Option Plan	22	420	683	1,261
<hr/>				
Amount of stock-based compensation expense, before income tax benefit	\$ 233	\$ 2,031	\$ 2,696	\$ 6,379
<hr/>				
Amount of related income tax benefit recognized	\$ 77	\$ 504	\$ 928	\$ 1,517
<hr/>				

Employee Stock Ownership Plan. Concurrent with the conversion from mutual to stock ownership, we established an ESOP for the benefit of our employees. The ESOP is a qualified pension plan under Internal Revenue Service guidelines that covers all full-time employees who have completed 1,000 hours of service. Upon formation, the ESOP purchased 1,806,006 shares of common stock issued in the initial public offering with the proceeds of an \$18,060,060 loan from the Company.

We account for our ESOP in accordance with Financial Accounting Standards Board (FASB) Statement of Position 93-6, *Employers Accounting for Employee Stock Ownership Plans*. Accordingly, expense is recognized based on the market value (average stock price) of shares scheduled to be released from the ESOP trust. The excess fair value of ESOP shares over cost is recorded as compensation expense but is not deductible for tax purposes. As shares are committed to be released from collateral, we report compensation expense equal to the average market price of the shares and the shares become outstanding for EPS computations. Our contributions and dividends on allocated and unallocated ESOP shares are used to pay down the loan. Accordingly, we have recorded the obligation with an offsetting amount of unearned compensation in stockholders' equity in the accompanying Consolidated Statements of Financial Condition.

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	At or for the Three Months Ended September 30,		At or for the Nine Months Ended September 30,	
	2008	2007	2008	2007
<i>(Dollars in thousands, except for share data)</i>				
Employee Stock Ownership Plan compensation expense	\$ 164	\$ 885	\$ 1,012	\$ 2,940
Employee Stock Ownership Plan shares allocated to employees	790,128	639,627	790,128	639,627
Employee Stock Ownership Plan shares unallocated	1,015,878	1,166,379	1,015,878	1,166,379
Fair value of Employee Stock Ownership Plan unallocated shares	\$ 5,211	\$ 30,874	\$ 5,211	\$ 30,874

Management Recognition and Retention Plan. We established the 2003 Management Recognition and Retention Plan (MRRP) which is a stock-based incentive plan. The shares awarded by the MRRP vest to participants at the rate of 20% per year. Compensation expense for this plan is being recorded over a 60-month period, using the straight-line amortization method adjusted for forfeitures, and is based on the market value of our stock as of the date the awards were made. Stockholders approved 903,003 shares to be granted under the MRRP and 85,283 shares are still available for future grants as of September 30, 2008. The following table summarizes shares of our common stock that were subject to award and have been granted pursuant to the MRRP as of September 30, 2008 and 2007:

	At or for the Three Months Ended September 30,		At or for the Nine Months Ended September 30,	
	2008	2007	2008	2007
Nonvested shares outstanding at beginning of period	21,370	176,220	168,720	328,940
Shares granted	10,000	--	15,370	--
Shares vested	--	--	(152,720)	(152,720)
Shares forfeited	--	--	--	--
Nonvested shares outstanding at end of period	31,370	176,220	31,370	176,220

Compensation expense related to the MRRP totaled \$47,000 and \$726,000 for the three-month periods ended September 30, 2008 and 2007, respectively. Compensation expense related to the MRRP totaled \$1.0 million and \$2.2 million for the nine-month periods ended September 30, 2008 and 2007, respectively. The weighted average grant date fair value of outstanding shares awarded by the MRRP was \$15.57 and \$18.64 at September 30, 2008 and 2007, respectively. As of September 30, 2008, we had \$324,000 of total unrecognized employee compensation expense related to unvested MRRP shares which are expected to be recognized over a weighted average period of 29 months. We realized excess tax benefits related to MRRP shares of zero and \$5,000 during the three months ended September 30, 2008 and 2007, respectively. We realized excess tax benefits related to MRRP shares of \$10,000 and \$378,000 during the nine months ended September 30, 2008 and 2007, respectively.

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Stock Option Plan. We established the 2003 Stock Option Plan (SOP) under which 2,257,508 shares of our common stock were reserved for the grant of stock options to directors, officers and employees. Stock options awarded under the SOP vest to participants at the rate of 20% per year. Compensation expense for this plan is being recorded over a 60-month period, using the straight-line amortization method adjusted for forfeitures, and is based on the fair value of our stock options as of the date the awards were made. The exercise price of the options is equal to the market price of the common stock on the grant date. Stockholders approved 2,257,508 stock options to be granted under the SOP and 349,758 of these stock options remain available for future grants as of September 30, 2008.

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The fair value of each option was estimated on the date of the grant using the Black-Scholes model. The dividend yield was calculated based on the annual dividends paid and the 12-month average closing stock price at the time of the grant. Expected volatility was based on historical volatility of our stock price at the date of grant. We have utilized historical experience to determine the expected life of the stock options and to estimate future forfeitures. All inputs into the Black-Scholes model are estimates at the time of the grant. Actual results in the future could materially differ from these estimates; however, such results would not impact future reported net income.

The following table details the inputs into the Black-Scholes model for stock options granted during the three and nine months ended September 30, 2008.

	Three and Nine Months Ended	
	September 30, 2008	
Dividend yield		0.50%
Expected volatility		46.03%
Risk-free interest rate		4.00%
Expected life of stock options		8 years
Weighted average fair value of stock options granted	\$	2.85

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Stock Option Activity. The following table details stock options granted, exercised and forfeited during the three months ended September 30, 2008:

<i>(Dollars in thousands, except per share data)</i>	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
Stock options outstanding at June 30, 2008	1,790,726	\$ 17.92		
Stock options granted	10,000	5.33		
Stock options exercised	--	--		
Stock options forfeited	(1,000)	--		
Stock options outstanding at September 30, 2008	1,799,726	\$ 17.85	4.6	\$ --
Stock options exercisable at September 30, 2008	1,775,726	\$ 17.88	4.6	\$ --

The following table details stock options granted, exercised and forfeited during the three months ended September 30, 2007:

<i>(Dollars in thousands, except per share data)</i>	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
--	---------------------	---------------------------------------	---	---------------------------------

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Stock options outstanding at June 30, 2007	1,798,226	\$	17.92		
Stock options granted	--		--		
Stock options exercised	--		--		
Stock options forfeited	--		--		
Stock options outstanding at September 30, 2007	1,798,226	\$	17.92	5.6	\$ 15,400
Stock options exercisable at September 30, 2007	1,410,676	\$	17.88	5.6	\$ 12,100

The following table details stock options granted, exercised and forfeited during the nine months ended September 30, 2008:

<i>(Dollars in thousands, except per share data)</i>	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
Stock options outstanding at December 31, 2007	1,792,226	\$ 17.92		
Stock options granted	10,000	5.33		
Stock options exercised	(1,000)	17.83		
Stock options forfeited	(1,500)	17.83		
Stock options outstanding at September 30, 2008	1,799,726	\$ 17.85	4.6	\$ --
Stock options exercisable at September 30, 2008	1,775,726	\$ 17.88	4.6	\$ --

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The following table details stock options granted, exercised and forfeited during the nine months ended September 30, 2007:

<i>(Dollars in thousands, except per share data)</i>	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value
Stock options outstanding at December 31, 2006	1,818,626	\$ 17.92		
Stock options granted	--	--		
Stock options exercised	(19,900)	17.83		
Stock options forfeited	(500)	17.83		
Stock options outstanding at September 30, 2007	1,798,226	\$ 17.92	5.6	\$ 15,400
Stock options exercisable at September 30, 2007	1,410,676	\$ 17.88	5.6	\$ 12,100

The following table details the intrinsic value, cash received and tax benefit realized from the exercise of stock options during the three and nine months ended September 30, 2008 and 2007:

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2008	2007	2008	2007
<i>(Dollars in thousands)</i>				
Intrinsic value (market value on the exercise date less the strike price)	\$ --	\$ --	\$ 5	\$ 228
Cash received from the exercise of stock options	--	--	18	355
Tax benefit realized from the exercise of stock options	--	--	--	50

At September 30, 2008, there was \$80,000 of total unrecognized compensation expense related to unvested stock options that will be expensed over a weighted average period of 29 months.

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Note 11 Unrecognized Tax Benefits

We adopted FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes – an Interpretation of FASB Statement No. 109*, on January 1, 2007 and, as a result, recognized no material adjustment in our liability for unrecognized tax benefits. Unrecognized tax benefits, excluding interest and penalties, were \$150,000 at September 30, 2008. Unrecognized tax benefits of \$147,000 and interest and penalties of \$8,000 would favorably affect our effective tax rate if recognized in future periods. The following table summarizes our unrecognized tax benefits for the nine months ended September 30, 2008:

<i>(Dollars in thousands)</i>	Unrecognized Tax Benefits
Unrecognized tax benefits at December 31, 2007	\$ 4,336
Changes in unrecognized tax benefits for the nine months ended: September 30, 2008	(127)
Changes in unrecognized tax benefits due to lapse of statute of limitations	(566)
Changes in unrecognized tax benefits related to deferred loan fees due to a change in a tax accounting method approved by the Internal Revenue Service	(3,493)
Unrecognized tax benefits at September 30, 2008	\$ 150

Any interest and penalties related to uncertain tax positions are recorded in income tax expense in the Consolidated Statements of Operations. At September 30, 2008, we had approximately \$8,000 of accrued interest payable related to uncertain tax positions recorded in our Consolidated Statements of Financial Condition.

We anticipate that a reduction in unrecognized tax benefits of up to \$32,000 is reasonably possible during the next 12 months. This potential reduction is primarily attributable to the expiration of the statute of limitations related to the 2005 tax period.

The tax years of 2005 through 2007 remain open for examination by federal and state taxing authorities.

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Note 12 Fair Value Measurements

Effective January 1, 2008, we adopted the provisions of SFAS No. 157, *Fair Value Measurements*, for financial assets and financial liabilities. In accordance with FASB Staff Position No. 157-2, *Effective Date of FASB Statement No. 157*, we delayed application of SFAS No. 157 for non-financial assets and non-financial liabilities until January 1, 2009. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in GAAP and expands disclosures about fair value measurements.

SFAS No. 157 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. A fair value measurement assumes that the transaction to sell the asset or transfer the liability occurs in the principal market for the asset or liability or, in the absence of a principal market, the most advantageous market for the asset or liability. The price in the principal (or most advantageous) market used to measure the fair value of the asset or liability shall not be adjusted for transaction costs. An orderly transaction is a transaction that assumes exposure to the market for a period prior to the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets and liabilities; it is not a forced transaction. Market participants are buyers and sellers in the principal market that are (a) independent, (b) knowledgeable, (c) able to transact, and (d) willing to transact.

SFAS No. 157 requires the use of valuation techniques that are consistent with the market approach, the income approach and/or the cost approach. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets and liabilities. The income approach uses valuation techniques to convert future amounts, such as cash flows or earnings, to a single present amount on a discounted basis. The cost approach is based on the amount that currently would be required to replace the service capacity of an asset (replacement cost). Valuation techniques should be consistently applied. Inputs to valuation techniques refer to the assumptions that market participants would use in pricing the asset or liability. Inputs may be observable, meaning those that reflect the assumptions market participants would use in pricing the asset or liability developed based on market data obtained from independent sources, or unobservable, meaning those that reflect the reporting entity's own assumptions about the assumptions market participants would use in pricing the asset or liability developed based on the best information available in the circumstances. In that regard, SFAS No. 157 establishes a fair value hierarchy for valuation inputs that gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

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The fair value hierarchy is as follows:

Level 1 Inputs Unadjusted quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2 Inputs Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These might include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (such as interest rates, volatilities, prepayment speeds, credit risks, etc.) or inputs that are derived principally from or corroborated by market data by correlation or other means.

Level 3 Inputs Unobservable inputs for determining the fair values of assets or liabilities that reflect an entity's own assumptions about the assumptions that market participants would use in pricing the assets or liabilities.

In general, fair value is based upon quoted market prices, where available. If such quoted market prices are not available, fair value is based upon internally developed models that primarily use, as inputs, observable market-based parameters. Valuation adjustments may be made to ensure that financial instruments are recorded at fair value. These adjustments may include amounts that reflect counterparty credit quality and creditworthiness, among other things, as well as unobservable parameters. Any such valuation adjustments are applied consistently over time. Our valuation methodologies may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. While management believes our valuation methodologies are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different estimate of fair value at the reporting date.

A description of the valuation methodologies used for instruments measured at fair value, as well as the general classification of such instruments pursuant to the valuation hierarchy, is set forth below. These valuation methodologies were applied to all of our financial assets and financial liabilities carried at fair value effective January 1, 2008.

The following disclosures exclude certain nonfinancial assets and liabilities which are deferred under the provisions of FASB Staff Position 157-2. These include foreclosed real estate, long-lived assets, goodwill and core deposit premiums, which are all written down to fair value upon impairment. The FASB's deferral is intended to allow additional time to consider the effect of various implementation issues relating to these non-financial instruments and defers disclosures under SFAS No. 157 until January 1, 2009.

TierOne Corporation and Subsidiaries
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Valuation methods for instruments measured at fair value on a recurring basis

The following is a description of our valuation methodologies used for instruments measured at fair value on a recurring basis:

Investment Securities, Available for Sale This portfolio comprises the majority of the assets which we record at fair value. Securities classified as available for sale, which include U.S. Government securities and agency obligations, corporate securities and Asset Management Fund, are priced utilizing observable data from an active market. These measurements are classified as Level 1.

Changes in the fair value of available for sale investment securities are included in other comprehensive income (loss) to the extent the changes are not considered other than temporary impairments. Other than temporary impairment tests are performed on a quarterly basis and any decline in the fair value of an individual security below its cost that is deemed to be other than temporary results in a write-down to estimated fair value. These write-downs are included as a component of earnings as realized losses. We recorded impairment charges of \$355,000 and \$949,000 during the three and nine months ended September 30, 2008, respectively.

Municipal obligations, mortgage-backed securities and agency equity securities are valued using a type of matrix, or grid, pricing in which securities are benchmarked against the treasury rate based on credit rating. These model and matrix measurements are classified as Level 2 in the fair value hierarchy.

Derivatives. Our derivative instruments are loan commitments and forward loan sales related to personal mortgage loan origination activity. The fair values of mortgage loan commitments and forward sales contracts are based on quoted prices for similar loans in the secondary market. However, these prices are adjusted by a factor which considers the likelihood that the commitment will ultimately result in a closed loan. Based on the unobservable nature of this adjustment, these measurements are classified as Level 3. The fair value of derivatives was \$151,000 and \$136,000 at September 30, 2008 and December 31, 2007, respectively. The \$15,000 change in the fair value amount is included in the gain on the sale of loans in the accompanying Consolidated Statements of Operations.

TierOne Corporation and Subsidiaries
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(Unaudited)

The following table summarizes financial assets and financial liabilities measured at fair value on a recurring basis as of September 30, 2008, segregated by the level of the valuation inputs within the fair value hierarchy utilized to measure fair value:

<i>(Dollars in thousands)</i>	Level 1 Inputs	Level 2 Inputs	Level 3 Inputs	Total Fair Value
Securities, available for sale:				
Mortgage-backed securities	\$ --	\$ 3,615	\$ --	\$ 3,615
U.S. Government securities and agency obligations	142,594	--	--	142,594
Corporate securities	3,605	--	--	3,605
Municipal obligations	--	11,983	--	11,983
Agency equity securities	--	23	--	23
Asset Management Fund - ARM Fund	4,906	--	--	4,906
Total investment securities, available for sale	151,105	15,621	--	166,726
SFAS No. 133 derivatives:				
Loan commitments	--	--	382	382
Forward loan sales	--	--	(231)	(231)
Total SFAS No. 133 derivatives	--	--	151	151
Total assets measured at fair value	\$ 151,105	\$ 15,621	\$ 151	\$ 166,877

Valuation methods for instruments measured at fair value on a nonrecurring basis

The following is a description of our valuation methodologies used for other financial instruments measured at fair value on a nonrecurring basis. Except as noted below for impaired loans, no fair value adjustments on these instruments were recognized in the current period.

Collateral Dependent Impaired Loans. While the overall loan portfolio is not carried at fair value, adjustments are recorded on certain loans to reflect partial write-downs that are based on the value of the underlying collateral. In determining the value of real estate collateral, we rely on external appraisals and assessment of property values by our internal staff. In the case of non-real estate collateral, reliance is placed on a variety of sources, including external estimates of value and judgments based on the experience and expertise of internal specialists. Because many of these inputs are not observable, the measurements are classified as Level 3. The carrying value of these impaired loans was \$158.1 million at September 30, 2008. Charge-offs on impaired loans during the three and nine months ended September 30, 2008 were \$7.3 million and \$78.2 million, respectively. The related allowance increased by \$328,000 for the three months ended September 30, 2008 and decreased by \$11.6 million for the nine months ended September 30, 2008, respectively. The allowance for loan losses related to impaired loans was \$13.0 million at September 30, 2008 compared to \$24.6 million at December 31, 2007.

TierOne Corporation and Subsidiaries
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Loans Held for Sale. Loans held for sale are carried at the lower of cost or market value. The portfolio consists primarily of fixed rate single-family residential real estate loans.

Single-family residential real estate loan measurements are based on quoted market prices for similar loans in the secondary market. These measurements are classified as Level 2 as they utilize quoted market prices for similar assets in an active market.

FHLBank Topeka Stock. At September 30, 2008, we held \$46.7 million of FHLBank Topeka stock which represents our carrying value which is approximately equal to fair value. Fair value measurements for these securities are classified as Level 3 based on their undeliverable nature related to credit risk.

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Mortgage Servicing Rights. We initially measure our mortgage servicing rights at fair value, and amortize them over the period of estimated net servicing income. They are periodically assessed for impairment based on fair value at the reporting date. Mortgage servicing rights do not trade in an active market with readily observable prices. Accordingly, the fair value is estimated based on a valuation model which calculates the present value of estimated future net servicing income. The model incorporates assumptions that market participants use in estimating future net servicing income, including estimates of prepayment speeds, market discount rates, cost to service, float earnings rates and other ancillary income, including late fees. The fair value measurements are classified as Level 3. A valuation allowance of \$76,000 was recorded as a reduction of fees and services charges during the nine months ended September 30, 2008. The valuation allowance was zero at December 31, 2007.

Effective January 1, 2008, we adopted the provisions of SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115*. SFAS No. 159 allows us to choose to measure eligible items at fair value at specified election dates. Unrealized gains and losses on items for which the fair value measurement option has been elected are reported in earnings at each subsequent reporting date. The fair value option (a) may be applied instrument by instrument, with certain exceptions, thus we may record identical financial assets and liabilities at fair value or by another measurement basis permitted under generally accepted accounting principals, (b) is irrevocable (unless a new election date occurs) and (c) is applied only to entire instruments and not to portions of instruments. Adoption of SFAS No. 159 on January 1, 2008 did not have any impact on our consolidated financial statements.

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

The following is a discussion and analysis of the Company's financial condition and results of operations including information on the Company's critical accounting policies, asset/liability management, liquidity and capital resources and contractual obligations. Information contained in this Management's Discussion and Analysis should be read in conjunction with the disclosure regarding Forward-Looking Statements and the risk factors described in Part 2, Item 1A. of this Quarterly Report on Form 10-Q.

General

TierOne Bank (Bank), a subsidiary of TierOne Corporation (Company), is a \$3.2 billion federally chartered stock savings bank headquartered in Lincoln, Nebraska. Established in 1907, the Bank offers customers a wide variety of full-service consumer, commercial and agricultural banking products and services through a network of 69 banking offices located in Nebraska, Iowa and Kansas. Product offerings include residential, commercial and agricultural real estate loans; consumer, construction, business and agricultural operating loans; warehouse mortgage lines of credit; consumer and business checking and savings plans; investment and insurance services; and telephone and internet banking.

Our results of operations are dependent primarily on net interest income, which is the difference between the interest earned on our assets, primarily our loan and securities portfolios, and our cost of funds, which consists of the interest paid on our deposits and borrowings. Our results of operations are also affected by our provision for loan losses, noninterest income, noninterest expense and income tax expense. Noninterest income generally includes fees and service charges, debit card fees, net income from real estate operations, net gain on sales of investment securities, loans held for sale and real estate owned and other operating income. Noninterest expense consists of salaries and employee benefits, occupancy, data processing, advertising and other operating expense. Our results of operations are significantly affected by general economic and competitive conditions, particularly changes in market interest rates and U.S. Treasury yield curves, governmental policies and actions of regulatory authorities.

As used in this report, unless the context otherwise requires, the terms we, us, or our refer to the Company and the Bank.

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Recent Developments

Termination of Acquisition Agreement. On May 17, 2007, we entered into and announced an Agreement and Plan of Merger (Merger Agreement) with CapitalSource Inc. and CapitalSource TRS Inc. On March 20, 2008, our Board of Directors terminated the Merger Agreement. Pursuant to the terms of the Merger Agreement, either party had the right to terminate the Merger Agreement if the proposed merger was not completed by February 17, 2008. No termination fee was payable by either company as a result of the termination of the Merger Agreement.

TransLand Financial Services Loan Sale. On June 25, 2008, we announced the sale of over 300 delinquent residential construction loans previously originated by TransLand Financial Services Inc. (TransLand), a Florida-based mortgage brokerage firm. This sale comprised \$12.7 million, net of charge-offs, of our total nonperforming residential construction loans.

Loan Production Office Closings. On June 30, 2008, we announced the closing of all of our loan production offices in an effort to focus our lending activity in our primary market area of Nebraska, Iowa and Kansas. We completed the closure of all of our loan production offices during the three months ended September 30, 2008. The lending offices that were closed were located in Phoenix, Arizona; Colorado Springs, Denver and Fort Collins, Colorado; Orlando, Florida; Minneapolis, Minnesota; Las Vegas, Nevada and Charlotte and Raleigh, North Carolina. We will continue to service loans made to existing customers. At the current time, customer transition and collection support functions for existing customers will continue in Charlotte, Las Vegas, Minneapolis and Orlando.

Board of Director Appointment. On September 22, 2008, we announced that Ann Lindley Spence had submitted her resignation as a director of the Company and the Bank. On that same day, to fill the vacancy created by Ms. Spence's retirement, the Company's Board of Directors appointed Samuel P. Baird as an independent director of the Company for a term expiring at the 2010 annual meeting of stockholders. Mr. Baird, who was Director of the Nebraska Department of Banking and Finance from 1999-2004, has over 35 years of experience in banking, real estate, insurance and law. Mr. Baird was also appointed to the Audit and Compensation Committees of the Company's Board of Directors as well as director of the Bank.

Regulatory Developments. As a result of operating losses which were reported during the previous four quarterly periods during the current economic downturn, the Company is subject to certain limitations imposed by the Office of Thrift Supervision (OTS). We are restricted from: (1) paying dividends, (2) repurchasing common stock, and (3) making any payments on trust preferred securities without the prior written notice of non-objection of the OTS. To support our capital position during the current period of market volatility, the Bank currently has no requests pending before the OTS to pay dividends or repurchase stock. The Company has also agreed with the OTS to contribute additional capital above levels required for the Bank to be deemed well-capitalized for regulatory purposes. The Company has contributed \$19.1 million to the Bank during the first nine months of 2008 and subsequent to September 30, 2008, contributed an additional \$10.0 million to the Bank. The Bank is required to maintain a ratio of 11.0% (as opposed to 10.0%) with respect to total risk-based capital to risk-weighted assets and a ratio of 8.5% (as opposed to 6.0%) with respect to Tier 1 capital to risk-weighted assets. As of September 30, 2008, the Bank exceeded these elevated ratios before the subsequent \$10.0 million capital contribution. See Item 2 - Management's Discussion and Analysis of Financial Condition and Results of Operations - Regulatory Capital.

Critical Accounting Policies

Various elements of our accounting policies, by nature, are inherently subject to estimation techniques, valuation assumptions and other subjective assessments. Our policies with respect to the methodologies used to recognize income, determine the allowance for loan losses, evaluating investment and mortgage-backed securities for impairment, evaluating goodwill and other intangible assets, valuation of mortgage servicing rights, valuation and measurement of derivatives and commitments, valuation of real estate owned and estimating income taxes are our most critical accounting policies. These policies are important to the presentation of our financial condition and results of operations, involve a higher degree of complexity and require management to make difficult and subjective judgments which often require assumptions or estimates about highly uncertain matters. The use of different judgments, assumptions and estimates could result in material differences in our reported financial condition and results of operations.

Income Recognition. We recognize interest income by methods that conform to U.S. generally accepted accounting principles (GAAP). In the event management believes collection of all or a portion of contractual interest on a loan has become doubtful, which generally occurs after a loan is contractually delinquent 90 days or more, we discontinue the accrual of interest and charge-off all previously accrued interest. Interest received on nonperforming loans is included in income only if principal recovery is reasonably assured. A nonperforming loan is restored to accrual status when it is brought current and the collectibility of the total contractual principal and interest is no longer in doubt.

Allowance for Loan Losses. We have identified the allowance for loan losses as a critical accounting policy where amounts are subject to material variation. This policy is significantly affected by our judgment and uncertainties and there is a likelihood that materially different amounts could 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:

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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, in management's belief, 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:

Assigning individual loans to specific risk levels (pass, special mention, substandard, doubtful and loss);

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Trends and levels of delinquent, nonperforming or impaired loans;
Trends and levels of charge-offs and recoveries;
Underwriting terms or guarantees for loans;
Impact of changes in underwriting standards, risk tolerances or other changes in lending practices;
Changes in the value of collateral securing loans;
Total loans outstanding and the volume of loan originations;
Type, size, terms and geographic concentration of loans held;
Changes in qualifications or experience of the lending staff;
Changes in local or national economic or industry conditions;
Number of loans requiring heightened management oversight;
Changes in credit concentration; and
Changes in regulatory requirements.