

COMMUNITY BANK SYSTEM INC

Form DEF 14A

April 07, 2005

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**SCHEDULE 14A INFORMATION**

**Proxy Statement Pursuant to Section 14(a)  
of the Securities Exchange Act of 1934**

Fixed by the registrant

Filed by a party other than the registrant.

Check the appropriate box:

- Preliminary Proxy Statement
- Confidential, for Use of the Commission Only (as permitted by Rule 14a-6(e)(2))**
- Definitive Proxy Statement
- Definitive Additional Materials
- Soliciting Material Pursuant to § 240.14a-12

**Community Bank System, Inc.**

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(Name of Registrant as Specified In Its Charter)

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(Name of Person(s) Filing Proxy Statement if other than the Registrant)

Payment of Filing Fee (Check the appropriate box):

- No fee required.
- Fee computed on table below per Exchange Act Rules 14a-6(i)(1) and 0-11.

(1) Title of each class of securities to which transaction applies:

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(3) Per unit price or other underlying value of transaction computed pursuant to Exchange Act Rule 0-11 (set forth the amount on which the filing fee is calculated and state how it was determined):

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(1) Amount Previously Paid: \_\_\_\_\_

(2) Form, Schedule or Registration Statement No.: \_\_\_\_\_

(3) Filing Party: \_\_\_\_\_

(4) Date Filed: \_\_\_\_\_

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COMMUNITY BANK SYSTEM, INC.

5790 Widewaters Parkway  
DeWitt, New York 13214-1883

**NOTICE OF ANNUAL MEETING OF SHAREHOLDERS**

April 7, 2005

**To the Shareholders of Community Bank System, Inc.:**

At the direction of the Board of Directors of **Community Bank System, Inc.**, a Delaware corporation (the Company ), ***NOTICE IS HEREBY GIVEN*** that the Annual Meeting of Shareholders of the Company (the Meeting ) will be held at 1:00 p.m. on Wednesday, May 11, 2005 at the Woodlands Inn & Resort in Wilkes-Barre, Pennsylvania for the purpose of considering and voting upon the following matters:

1. The election of four directors to hold office for a term of three years and until their successors have been duly elected.
2. The transaction of any other business which may properly be brought before the Meeting or any adjournment thereof.

By Order of the Board of Directors

Donna J. Drengel  
Secretary

**YOUR VOTE IS IMPORTANT. YOU ARE THEREFORE REQUESTED TO SIGN AND RETURN THE ENCLOSED PROXY CARD AS PROMPTLY AS POSSIBLE, EVEN IF YOU EXPECT TO BE PRESENT AT THE MEETING. YOU MAY WITHDRAW YOUR PROXY AT ANY TIME PRIOR TO THE MEETING, OR IF YOU DO ATTEND THE MEETING, YOU MAY WITHDRAW YOUR PROXY AT THAT TIME AND VOTE IN PERSON IF YOU WISH.**

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COMMUNITY BANK SYSTEM, INC.

5790 Widewaters Parkway  
DeWitt, New York 13214-1883

**PROXY STATEMENT**

**FOR ANNUAL MEETING OF SHAREHOLDERS, MAY 11, 2005**

This Proxy Statement is furnished as part of the solicitation of proxies by the Board of Directors of Community Bank System, Inc. (the Company), the holding company for Community Bank, N.A. (the Bank), for use at the Annual Meeting of Shareholders of the Company (the Meeting) to be held at 1:00 p.m. on Wednesday, May 11, 2005, at the Woodlands Inn & Resort in Wilkes-Barre, Pennsylvania. This Proxy Statement and the form of Proxy are first being sent to Shareholders on approximately April 7, 2005.

At the Meeting, the Shareholders will be asked to vote for the election of directors. Four of the total of thirteen directors who serve on the Company's Board of Directors (excluding current directors whose terms will not continue after the Meeting) will stand for re-election to the Board at the Meeting. In addition, voting will be conducted on any other matters which are properly brought before the Meeting.

**VOTING RIGHTS AND PROXIES**

The Board of Directors of the Company has fixed the close of business on March 23, 2005 as the record date for determining which Shareholders are entitled to notice of and to vote at the Meeting. At the close of business on the record date, 30,322,110 shares of common stock, \$1.00 par value, were outstanding and entitled to vote at the Meeting. This is the Company's only class of voting stock outstanding. Each share of outstanding common stock is entitled to one vote with respect to each item to come before the Meeting. There will be no cumulative voting of shares for any matter voted upon at the Meeting. The Bylaws of the Company provide that one-third of the outstanding shares of the Company, represented in person or by proxy, shall constitute a quorum at a shareholder meeting.

If the enclosed form of Proxy is properly executed and returned to the Company prior to or at the Meeting, and if the Proxy is not revoked prior to its exercise, all shares represented thereby will be voted at the Meeting and, where instructions have been given by a Shareholder, will be voted in accordance with such instructions.

Any Shareholder executing a Proxy which is solicited hereby has the power to revoke it at any time prior to its exercise. A Proxy may be revoked by giving written notice to the Secretary of the Company at the Company's address set forth above, by attending the Meeting and voting the shares of stock in person, or by executing and delivering to the Secretary a later-dated Proxy.

The Company will bear all costs of soliciting Proxies. The solicitation of Proxies will be by mail, but Proxies may also be solicited by telephone, telegram, or in person by directors, officers, and other regular employees of the Company or of the Bank. Should the Company, in order to solicit Proxies, request the assistance of other financial institutions, brokerage houses, or other custodians, nominees, or fiduciaries, the Company will reimburse such persons for their reasonable expenses in forwarding proxy materials to Shareholders and obtaining their Proxies.



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The Annual Report of the Company for the fiscal year ended December 31, 2004, incorporating the Annual Report on Form 10-K filed by the Company with the Securities and Exchange Commission, is being sent to Shareholders with this Proxy Statement.

**SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS**

The following table sets forth certain information with respect to persons known to the Company to own beneficially more than 5% of the outstanding shares of common stock of the Company as of March 23, 2005 (except as otherwise indicated).

<b>Name and Address of Beneficial Owner</b>	<b>Number of Shares of Common Stock Beneficially Owned</b>	<b>Percent of Class</b>
Barclays Global Investors, NA/ Barclays Global Fund Advisors 45 Fremont Street San Francisco, CA 94105	1,707,651 (1)	5.63%

- (1) Based solely on information contained in Schedule 13G filed with the Securities and Exchange Commission on February 14, 2005, Barclays Global Investors, NA and Barclays Global Fund Advisors collectively have sole voting power with respect to 1,568,621 shares and sole dispositive power with respect to all shares listed.

**ITEM 1: ELECTION OF DIRECTORS AND INFORMATION WITH  
RESPECT TO DIRECTORS AND EXECUTIVE OFFICERS**

The first Item to be acted upon at the Meeting is the election of four directors, each to hold office for three years and until his successor shall have been duly elected and qualified. Pursuant to the Company's Bylaws, William N. Sloan retired from the Board effective as of December 31, 2004. In addition, Saul Kaplan, whose term of office expires as of the date of the Meeting, will not stand for reelection at the Meeting. As a result, Lee T. Hirschey, who is presently serving a term of office to expire in 2006, will stand for election with the other nominees listed below (each of whom is presently serving a term of office to expire as of the date of the Meeting) in order to maintain membership among the three classes as nearly equal as possible in accordance with the Company's Certificate of Incorporation and Bylaws. The nominees receiving a plurality of the votes represented in person or by proxy at the Meeting will be elected directors.

All Proxies in proper form which are received by the Board prior to the election of directors at the Meeting will be voted FOR the nominees listed below, unless authority is withheld in the space provided on the enclosed Proxy. Each nominee is presently a director of the Company, and each director of the Company is also a director of the Bank. In the event any nominee declines or is unable to serve, it is intended that the Proxies will be voted for a successor nominee designated by the Board. All nominees have indicated a willingness to serve, and the Board knows of no reason to believe that any nominee will decline or be unable to serve if elected. The thirteen members of the Board whose terms will continue beyond the meeting (including the nominees for re-election at the Meeting, if elected) are expected to continue to serve on the Board until their respective terms expire.

The information set forth below is furnished for each nominee for director to be elected at the Meeting and each director of the Company whose term of office continues after the Meeting. The share ownership numbers for certain directors include shares that would be issuable upon exercise of Offset Options granted to these directors in order to reduce the Company's liability under its Stock Balance Plan. The purpose of the Offset Options is explained on pages 10-11. See footnote (e) on page 6 for the number of currently exercisable stock options (including, without limitation, Offset Options) held by specific directors.





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<b>Name and Age (a)</b>	<b>Director of the Company Since</b>	<b>Business Experience During Past Five Years (b)</b>	<b>Shares of Company Common Stock Beneficially Owned (c) as of March 23, 2005 (d)</b>	
			<b>Number(e)</b>	<b>Percent</b>
<b>Nominees (for terms to expire at Annual Meeting in 2008):</b>				
Brian R. Ace (f) Age 50	2003	Owner, Laceyville Hardware, Laceyville, Pennsylvania.	53,484	.18%
Paul M. Cantwell, Jr. Age 63	2001	Owner, law firm of Cantwell & Cantwell, Malone, New York. Prior to January 2001, Chairman and President, The Citizens National Bank of Malone.	123,650	.41%
William M. Dempsey Age 66	1984	Retired. Prior to 2001, Assistant to the President, Rochester Institute of Technology, Rochester, New York; President/Dean, American College of Management and Technology (RIT), Dubrovnik, Croatia (August 1997 - July 1999); prior to August 1997, Vice President of Finance and Administration, RIT.	111,719	.37%
Lee T. Hirschey Age 69	1991	Chairman and Chief Executive Officer, Climax Manufacturing Company, converter and manufacturer of paper products with facilities in Castorland, Lowville, and West Carthage, New York.	90,200	.30%

**Directors Continuing in Office****Terms Expiring at Annual Meeting in 2006:**

Sanford A. Belden Age 62	1992	President and Chief Executive Officer of the Company.	106,683	.35%
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Name and Age (a)	Director of the Company Since	Business Experience During Past Five Years (b)	Shares of Company Common Stock Beneficially Owned (c) as of March 23, 2005 (d)	
			Number(e)	Percent
David C. Patterson Age 63	1991	President and owner of Wight and Patterson, Inc., manufacturer and seller of livestock feed located in Canton, New York.	125,566	.41%
Peter A. Sabia (h) Age 73	2001	Owner, Valley Dodge Truck Center, Dunmore, Pennsylvania.	260,765	.86%
Sally A. Steele (f) Age 49	2003	Attorney, self-employed as general practitioner with concentration in real estate and elder law, Tunkhannock, Pennsylvania.	47,838	.16%
<b>Terms expiring at Annual Meeting in 2007:</b>				
John M. Burgess Age 68	1991	Retired. Prior to 1991, President of Kinney Drugs, Inc., a drug and retail chain with stores located throughout northern New York.	98,832	.33%
Nicholas A. DiCerbo Age 58	1984	Partner, law firm of DiCerbo and Palumbo, Olean, New York.	274,982	.90%
James A. Gabriel Age 57	1984	Owner, law firm of Franklin & Gabriel, Ovid, New York	178,884	.59%
Harold Kaplan (h) Age 71	2001	Co-owner, M.C.F., Inc., and Partner, D&T Real Estate, Scranton, Pennsylvania. Prior to April 2003, Co-Owner, Montage Foods, Inc., Scranton, Pennsylvania.	293,952	.97%
Charles E. Parente (g) Age 64	2004	Chief Executive Officer of Pagnotti Enterprises, Inc., a diversified holding company whose primary business includes workers compensation insurance, real estate, anthracite coal mining preparation and sales, and cable television.	199,462	.66%

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In addition to the information provided above, the following summarizes the security ownership of the highest paid executive officers who are not also directors of the Company:

		<b>Shares of Company Common Stock Beneficially Owned (c) as of March 23, 2005 (d)</b>	
		<b>Number (e)</b>	<b>Percent</b>
James A. Wears Age 55	President, New York Banking	83,114	.27%
Michael A. Patton Age 59	President, Financial Services	143,380	.47%
Mark E. Tryniski Age 44	Executive Vice President/ Chief Operating Officer	7,534	.02%
Thomas A. McCullough Age 58	President, Pennsylvania Banking	79,825	.26%
Number of shares of Company common stock beneficially owned by all directors, persons chosen to become directors and executive officers of the Company as a group (28 persons)		2,519,708	8.08%

- (a) No family relationships exist between any of the aforementioned directors or executive officers of the Company.
- (b) No nominee for director or continuing director of the Company holds a directorship with any company (other than the Company) which is registered pursuant to Section 12 or subject to the requirements of Section 15(d) of the Securities Exchange Act of 1934, or with any company which is a registered investment company under the Investment Company Act of 1940.
- (c) Represents all shares as to which named individual possessed sole or shared voting or investment power as of March 23, 2005. Includes shares held by, in the name of, or in trust for, spouse and dependent children of named individual and other relatives living in the same household, even if beneficial ownership has been disclaimed as to any of these shares by the nominee or director.
- (d) The listed amounts include shares as to which certain directors and named executive officers are beneficial owners but not the sole beneficial owners as follows: Mr. Belden is the beneficial owner of 2,131 shares held by the Company's 401(k) plan; Mr. Burgess's wife holds 7,200 shares; Mr. Cantwell's wife holds 10,200 shares; Mr. DiCerbo holds 59,832 shares jointly with his wife, 86,005 shares are held in the name of the law partnership of DiCerbo and Palumbo, and 1,667 shares are held by his wife; Mr. Hirschey's wife holds 2,000 shares, and Mr. Hirschey holds 26,080 shares as Trustee for the Retirement Plan of Employees of Climax Manufacturing Company and 700 shares as Trustee of an Internal Revenue Code Section 2503C trust; 86,576 shares are held by a limited partnership controlled by Mr. Kaplan, and 4,000 shares are held by a charitable foundation of which Mr. Kaplan serves as President, Treasurer, and Director; Mr. McCullough holds 108 shares jointly with his spouse and 630 shares jointly with his mother, and his children hold 222 shares; Mr. Parente holds 10,000 shares as Trustee of the C.E. Parente Trust U/A, his wife holds 3,000 shares, and 182,858 shares are held by a partnership controlled by Mr. Parente; Mr. Patterson holds 4,760 shares jointly with his wife, and

3,276 shares as Trustee for the Wight and Patterson Retirement Plan; Mr. Patton is the beneficial owner of 8,198 shares held by the Company's 401(k) plan, and his wife holds 2,800 shares; Mr. Sabia holds 180,000 shares as Trustee for the Peter A. Sabia Trust U/A, he holds 6,120 shares as Trustee for the Sabia Family

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Foundation, and 58,747 shares are held by Valley Dodge Truck Center, of which Mr. Sabia is owner; Ms. Steele holds 42,514 shares jointly with her husband; and Mr. Wears is the beneficial owner of 10,872 shares held by the Company's 401(k) plan, he holds 6,234 shares jointly with his wife, and his children hold 5,398 shares.

- (e) Includes shares that the following individuals currently have the right to acquire, or will have the right to acquire within 60 days of March 23, 2005, through exercise of stock options issued by the Company: Mr. Ace, 24,710 shares; Mr. Belden, 12,324 shares; Mr. Burgess, 71,192 shares; Mr. Cantwell, 12,924 shares; Mr. Dempsey, 108,496 shares; Mr. DiCerbo, 110,932 shares; Mr. Gabriel, 111,562 shares; Mr. Hirschey, 48,736 shares; Mr. Kaplan, 8,124 shares; Mr. Parente, 3,604 shares; Mr. Patterson, 102,254 shares; Mr. Patton, 54,888 shares; Mr. Sabia, 3,604 shares; Ms. Steele, 3,604 shares; Mr. Tryniski, 5,934 shares; and Mr. Wears, 60,610 shares. These shares are included in the total number of shares outstanding for the purpose of calculating the percentage ownership of the foregoing individuals and of the group as a whole, but not for the purpose of calculating the percentage ownership of other individuals listed in the foregoing table.
- (f) Pursuant to the terms of a Merger Agreement dated as of June 7, 2003 providing for the merger of Grange National Banc Corp. ( Grange ) with and into the Company (which merger was consummated in November 2003), the Company agreed to appoint two of Grange's former directors, Brian R. Ace and Sally A. Steele, to serve as members of its Board of Directors for terms expiring at the 2005 and 2006 annual Shareholders meetings, respectively.
- (g) Pursuant to the terms of a Merger Agreement dated as of March 11, 2004 providing for the merger of First Heritage Bank with and into the Bank (which merger was consummated in May 2004), the Company agreed to appoint one of First Heritage Bank's former shareholders, Charles E. Parente, to serve as a member of the Company's Board of Directors for a term expiring at the 2007 annual Shareholders meeting. The Merger Agreement further provided that, subject to the exercise of the Board's fiduciary duty, Mr. Parente would be nominated for at least one additional three-year term upon expiration of his initial term, and that the Board would recommend that the Company's Shareholders vote in favor of his reelection.
- (h) Pursuant to the terms of a Merger Agreement dated as of November 29, 2000 providing for the merger of First Liberty Bank Corp. ( First Liberty ) with and into the Company (which merger was consummated in May 2001), the Company agreed to appoint three of First Liberty's former directors, Saul Kaplan, Peter A. Sabia, and Harold Kaplan, to serve as members of its Board of Directors for terms expiring at the 2002, 2003, and 2004 annual Shareholders meetings, respectively. The Merger Agreement further provided that, subject to the exercise of the Board's fiduciary duty, Messrs. Kaplan, Sabia, and Kaplan would be nominated for at least one additional three-year term upon expiration of these initial terms, and that the Board would recommend that the Company's Shareholders vote in favor of their reelection. Saul Kaplan's current term of office will expire as of the date of the Meeting, and he will not stand for reelection.

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**BOARD COMPOSITION, MEETINGS, COMMITTEES, AND COMPENSATION**

**Independence**

The Company has adopted a set of Corporate Governance Guidelines, a copy of which is available on the Company's website at [www.communitybankna.com](http://www.communitybankna.com). The Corporate Governance Guidelines require that the Company's Board of Directors have at all times a majority of directors who meet the criteria for independence established by the New York Stock Exchange ( NYSE ), and the Board currently meets this requirement.

Under the NYSE rules, to be considered independent, the Board must determine that a director does not have a direct or indirect material relationship with the Company. Moreover, a director will not be independent if, within the preceding three years: (i) the director was employed by the Company or receives \$100,000 per year in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation for prior service, (ii) the director was a partner of or employed by the Company's independent auditor, (iii) the director is part of an interlocking directorate in which an executive officer of the Company serves on the compensation committee of another company that employs the director, (iv) the director is an executive officer or employee of another company that makes payments to, or receives payments from, the Company for property or services in an amount which, in any single fiscal year, exceeds the greater of \$1 million or 2% of the other company's consolidated gross revenues, or (v) the director had an immediate family member in any of the categories in (i)-(iv).

The Board has determined that 11 of the 14 current directors are independent under the NYSE standards. The independent directors are Brian R. Ace, John M. Burgess, William M. Dempsey, James A. Gabriel, Lee T. Hirschey, Harold S. Kaplan, Saul Kaplan, David C. Patterson, Charles E. Parente, Peter A. Sabia, and Sally A. Steele. In determining whether a director is independent, the Board relies on the NYSE numeric threshold standards as the primary factor in determining whether a director has any material relationship with the Company, but also considers whether a director has any relationships not meeting the NYSE thresholds that would otherwise interfere with the exercise of his or her independence from management and the Company. During the course of a year, directors are expected to inform the Board of any material changes in their circumstances or relationships that may impact their status or designation by the Board as independent.

Pursuant to the Corporate Governance Guidelines, the Company's independent directors meet in executive session at least quarterly, without the Company's management and non-independent directors present. The director who presides at these meetings is determined by the Board on the recommendation of the Nominating and Corporate Governance Committee.

**Director Meeting Attendance**

The Board of Directors held 12 regularly scheduled meetings and one special meeting during the fiscal year ended December 31, 2004. During this period, each director of the Company attended at least 75% of the aggregate of the total number of meetings of the Board and the total number of meetings held by committees of the Board on which he or she served.

The Company encourages all directors to attend each annual meeting of Shareholders. All of the then 15 incumbent directors attended the Company's last annual meeting of Shareholders held on May 19, 2004.

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**Board Committees**

Among its standing committees, the Board of the Bank has an Audit/Compliance/Risk Management Committee which also serves as the Company's Audit Committee. As described more fully on page 24, the Audit/Compliance/Risk Management Committee reviews internal and external audits of the Company and the Bank and the adequacy of the Company's and the Bank's accounting, financial, and compliance controls, and investigates and makes recommendations to the Company's Board and the Bank's Board regarding the appointment of independent auditors. The Audit/Compliance/Risk Management Committee held eight meetings during 2004, and its present members are Directors William M. Dempsey (Chair), John M. Burgess, Lee T. Hirschey, and Charles E. Parente.

The Bank's Board also has a Compensation Committee which reviews and makes recommendations to the Bank's Board regarding compensation adjustments and employee benefits to be instituted, and which also serves as the Company's Compensation Committee. As described more fully on pages 20-22, the Compensation Committee reviews the compensation of nonofficer employees in the aggregate, and the salaries and performance of executive officers are reviewed individually. The Compensation Committee held six meetings in 2004, and its present members are Directors Lee T. Hirschey (Chair), Brian R. Ace, David C. Patterson, and Peter A. Sabia.

The Company has a Nominating and Corporate Governance Committee which makes recommendations to the Board for nominees to serve as Directors. The Nominating and Corporate Governance Committee held four meetings in 2004, and its present members are Directors William M. Dempsey (Chair), Brian R. Ace, John M. Burgess, Lee T. Hirschey, and David C. Patterson. The Board has determined that each of the Nominating and Corporate Governance Committee's members is independent as defined by the NYSE Rules.

The Nominating and Corporate Governance Committee will consider written recommendations from Shareholders for nominees to serve on the Board that are sent to the Secretary of the Company at the Company's main office. In considering candidates for the Board, the Nominating and Corporate Governance Committee and the Board consider the entirety of each candidate's credentials and do not have any specific minimum qualifications that must be met by a nominee. Factors considered include, but are not necessarily limited to, outstanding achievement in a candidate's personal career; broad experience; wisdom; integrity; ability to make independent, analytical inquiries; understanding of the business environment; and willingness to devote adequate time to Board duties. The Board believes that each director should have a basic understanding of (i) the principal operational and financial objectives and plans and strategies of the Company, (ii) the results of operations and financial condition of the Company and of any significant subsidiaries or business segments, and (iii) the relative standing of the Company and its business segments in relation to its competitors. Prior to nominating an existing director for re-election to the Board, the Board and the Nominating and Corporate Governance Committee consider and review, among other relevant factors, the existing director's meeting attendance and performance, length of Board service, ability to meet regulatory independence requirements, and the experience, skills, and contributions that the director brings to the Board. The Nominating and Corporate Governance Committee has adopted a written charter setting forth its composition and responsibilities, a copy of which is available at the Company's website at [www.communitybankna.com](http://www.communitybankna.com).

The President and Chief Executive Officer of the Company serves as an ex officio member of all Board committees except the Audit/Compliance/Risk Management Committee, the Compensation Committee, and the Nominating and Corporate Governance Committee, and receives no compensation for serving in this capacity. Mr. Gabriel, as Chair of the Board, also serves as a member of all Board Committees except the Audit/Compliance/Risk Management Committee, the Compensation Committee, and the Nominating and Corporate Governance Committee.



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### **Communication with Directors**

Shareholders may communicate directly with the Board of Directors of the Company by sending correspondence to the address shown below. The receipt of any such correspondence addressed to the Board of Directors and the nature of its content will be reported at the next Board meeting and appropriate action, if any, will be taken. If a Shareholder desires to communicate with a specific director, the correspondence should be addressed to that director. Correspondence addressed to a specific director will be delivered to the director promptly after receipt by the Company. The director will review the correspondence received and, if appropriate, report the receipt of the correspondence and the nature of its content to the Board of Directors at its next meeting, so that the appropriate action, if any, may be taken.

Correspondence should be addressed to:

Community Bank System, Inc.  
Attention: [Board of Directors or Specific Director]  
5790 Widewaters Parkway  
DeWitt, New York 13214-1883

### **Compensation of Directors**

As directors of both the Company and the Bank, Board members receive an annual retainer of \$10,000, \$750 for each Board meeting they attend, and \$500 for each committee meeting they attend. Mr. Belden does not receive an annual retainer or compensation for attending Board and committee meetings. The Chair of the Board receives an all inclusive \$55,000 retainer for serving in that capacity. The Chair of the Audit/Compliance/Risk Management Committee receives an annual retainer of \$5,000; the Chairs of the Loan Committee, the Compensation Committee, and the Strategic/Executive Committee each receive an annual retainer of \$3,500; and the Chairs of the Investment Committee, the Nominating and Corporate Governance Committee, the Operations/Technology Committee, and the Trust Committee each receive an annual retainer of \$1,000. The Company pays the travel expenses incurred by each director in attending meetings of the Board.

Directors may elect to defer all or a portion of their director fees pursuant to a Deferred Compensation Plan for Directors. Directors who elect to participate in the Plan designate the percentage of their director fees which they wish to defer (the deferred fees ) and the date to which they wish to defer payment of benefits under the plan (the distribution date ). The plan administrator establishes an account for each participating director and credits to such account (i) on the date a participating director would have otherwise received payment of his or her deferred fees, the number of deferred shares of Company common stock which could have been purchased with the deferred fees, and (ii) from time to time such additional number of deferred shares which could have been purchased with any dividends which would have been received had shares equal to the number of shares credited to the account actually been issued and outstanding. On the distribution date, the participating director shall be entitled to receive shares of Company common stock equal to the number of deferred shares credited to the director's account either in a lump sum or in annual installments over a three, five or ten year period. The effect of the plan is to permit directors to invest deferred director fees in stock of the Company, having the benefit of any stock price appreciation and dividends as well as the risk of any decrease in the stock price. To the extent that directors participate in the plan, the interests of participating directors will be more closely associated with the interests of Shareholders in achieving growth in the Company's stock price.

Consistent with the Blue Ribbon Report issued by the National Association of Corporate Directors, which suggests that director compensation be structured so that it is specifically aligned with the long-term interests of Shareholders,

the Company's 2004 Long-Term Incentive Compensation Program (the 2004 Incentive Plan ) allows for the issuance of Non-Statutory Stock Options to nonemployee directors.

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The Board believes that providing for the grant of Non-Statutory Stock Options to nonemployee directors is in the best interests of the Company. In the spirit of the Blue Ribbon Report, such a provision more closely aligns the interests of individual directors with the long-term interests of the Company's Shareholders, and enables the Company to continue to attract qualified individuals to serve on the Board. In particular, when directors receive equity-based compensation such as stock options, their overall compensation is enhanced when the market price of the Company's common stock increases and is adversely affected when the market price of the Company's common stock decreases.

The 2004 Incentive Plan provides that each eligible nonemployee director is to receive an option to purchase 2,320 shares of common stock on or about January 1st of his or her first year as a director, and an option to purchase 4,000 shares on or about each January 1 thereafter. Each option granted to a nonemployee director is granted at an option price per share equal to the market value per share of the Company's common stock on the date of grant, and is fully exercisable on its date of grant, provided that shares of common stock acquired pursuant to the exercise of such options may not be sold or otherwise transferred by a director within six months of the grant. Each option is exercisable until the earlier of (i) ten years from the date of grant, or (ii) termination of the optionee's service on the Board for cause (as defined in the 2004 Incentive Plan). Notwithstanding the foregoing, to the extent that the Committee appointed by the Board to administer the 2004 Incentive Plan determines that grants may be exempt from Section 16(b) of the Securities Exchange Act of 1934, as amended, the Non-Statutory Stock Options granted to eligible nonemployee directors shall relate to a number of shares of common stock to be determined based upon the financial performance of the Company. Such financial performance shall be determined based upon factors including (but not limited to) the Company's growth in earnings per share, asset quality, return on equity, and CAMELS rating (a measurement of capital, assets, management, earnings, liquidity, and sensitivity utilized by the Office of the Comptroller of the Currency, the Bank's primary regulator). Pursuant to the 2004 Incentive Plan, each eligible nonemployee director received an option to purchase 4,520 shares effective January 21, 2004.

In addition, in keeping with the spirit of the Blue Ribbon Report, effective January 1, 1996, the Board adopted a Stock Balance Plan for nonemployee directors of the Company who have completed at least six months of service as director. The plan establishes an account for each eligible director. Amounts credited to those accounts reflect the value of 200 shares of the Company's common stock for each year of service between 1981 and 1995 at the December 31, 1995 market value, plus an annual amount equal to 200 additional shares of common stock beginning in 1996, plus an annual earnings credit equal to the one-year average total return on the Company's common stock. The crediting of additional units beginning in 1996 is subject to an adjustment factor which reflects the Company's asset quality, return on equity, and CAMELS rating. The account balance is payable to each director in the form of a lifetime annuity or, at the election of the director, monthly installment payments over a three, five, or ten year period following the later of age 55 or disassociation from the Board, is subject to a six-year vesting schedule, and is forfeitable in the event of termination from the Board for cause.

The 2004 Incentive Plan allows the grant of Offset Options to directors. The effect of these Offset Options is to permit the Company to reduce the grantee's Stock Balance Plan account balance by an amount equal to the growth in value of the Offset Options (i.e., the amount by which the aggregate fair market value of the common stock underlying the Offset Options exceeds the aggregate exercise price of the Offset Options) as of the date on which the director's account is valued, provided that a director's account may not be reduced below zero. As such, the Offset Options are not intended to materially change the level of compensation to participating directors under the Stock Balance Plan, but are intended to reduce the cost of director compensation to the Company. In the event that the growth in value of a director's Offset Options is less than the value of the director's Stock Balance Plan account as of the date that the Offset Options are exercised, the shortfall will be paid to the director either in cash or, at the Company's option in the case of an exercise prior to retirement, by the issuance of additional Offset

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Options. In the event that the growth in value of a director's Offset Options exceeds the value of the director's Stock Balance Plan account, no adjustment will be made.

The Bank has a consulting agreement with Paul M. Cantwell, Jr., a director of the Company and the Bank and the former Chairman and President of Citizens National Bank of Malone. Under this agreement, Mr. Cantwell will provide consulting services to the Bank until January 26, 2006 to facilitate the transition of Citizens National Bank's business and operations to the Bank, develop new business opportunities in the market areas formerly served by Citizens National Bank, and advise the Bank regarding corporate and business matters. Mr. Cantwell will provide these services on a part-time basis (not to exceed 250 hours per year), and will be paid \$50,000 per year. This amount is to be paid on a grossed-up basis for any Medicare and social security taxes (but not federal, state or local income taxes) payable by Mr. Cantwell on the amount. This means that in effect the Company will pay his Medicare and social security taxes. Pursuant to the agreement, the Bank has also agreed to pay the premiums for a life insurance policy for Mr. Cantwell's beneficiaries. This policy must provide coverage for no less than the remaining payments due under the consulting agreement. Finally, the Bank will make available health insurance coverage for Mr. Cantwell and his spouse on the same basis as its employees until age 65 and, thereafter, on the same basis as other retirees of the Bank.

**Table of Contents****COMPENSATION OF EXECUTIVE OFFICERS**

The following table sets forth information concerning compensation paid to those persons who served as chief executive officer (or in an equivalent capacity) during 2004 and to the other most highly compensated executive officers whose annual salary and bonus earned during 2004 exceeded \$100,000.

**SUMMARY COMPENSATION TABLE**

Name and Principal Position	Year	Annual Compensation		Long-Term Compensation Awards			All Other Compensation (\$) <sup>(4)</sup>
		Salary (\$)	Bonus (\$) (1)	Other Annual Compensation (\$) <sup>(2)</sup>	Restricted Stock Awards (\$) <sup>(3)</sup>	Stock Options (#)	
Sanford A. Belden President and Chief Executive Officer	2004	522,648	261,324	4,860	0	43,158	399,847
	2003	503,758	287,847	5,303	0	47,754	493,198
	2002	485,550	242,775	5,055	0	52,680	361,997
James A. Wears President, New York Banking	2004	228,238	68,471	5,285	0	14,676	118,886
	2003	219,988	89,557	4,676	0	15,114	87,546
	2002	188,926	54,900	3,555	0	17,290	39,008
Michael A. Patton President, Financial Services	2004	228,238	68,471	3,491	0	14,676	76,419
	2003	219,988	89,557	3,512	0	15,114	99,679
	2002	188,926	54,900	2,746	0	17,290	51,271
Mark E. Tryniski (5) Executive Vice President/ Chief Operating Officer	2004	250,002	75,000	5,368	0	14,676	17,359
	2003	129,808	53,432	2,125	0	0	277
Thomas A. McCullough (5) President, Pennsylvania Banking	2004	192,500	123,125	2,426	4,780	0	365,572
	2003	17,788	430,000	0	0	0	294

(1) The amounts shown in this column for Messrs. Belden, Wears, Patton, and Tryniski reflect payments under the Company's Management Incentive Plan, an annual cash award plan based on performance and designed to provide incentives for employees. The amounts shown in this column for Mr. McCullough reflect: (a) for 2004, an award under the Management Incentive Plan and payment of a \$75,000 retention bonus pursuant to the terms of the Grange acquisition, and (b) for 2003, payment of a signing bonus to Mr. McCullough in satisfaction of obligations to him under his former employment agreement with Grange.

(2) The amounts disclosed in this column include the reportable value of the personal use of Company-owned vehicles for Messrs. Belden, Wears, Patton, Tryniski, and McCullough.

(3) Indicates dollar value of restricted stock awards based upon the market value of the company stock on the date of grant. As of December 31, 2004, Mr. McCullough held 200 shares of restricted stock with a then current market value of \$5,650. Grantees of restricted stock entitled to receive dividends payable on their restricted stock holdings. The 200 shares of restricted stock granted to Mr. McCullough on August 18, 2004 vest in two equal installments on January 1, 2005 and January 1, 2006.

(4) The amounts in this column include: (a) the value of group term life insurance benefits in excess of \$50,000 under a plan available to all full-time employees for which Messrs. Belden, Wears, Patton, Tryniski, and McCullough received \$4,357, \$1,962, \$1,962, \$547, and \$1,092 in 2004, respectively; (b) Company contributions to the Employee Savings and Retirement Plan, a defined contribution plan, amounting to \$6,150 for Mr. Belden, \$6,150 for Mr. Wears, \$6,150 for Mr. Patton, \$3,250 for Mr. Tryniski, and \$3,323 for Mr. McCullough in 2004, respectively; (c) Company contributions under the Company's Deferred Compensation Plan, amounting to \$26,753 for Mr. Belden, \$12,639 for Mr. Wears, \$12,639 for Mr. Patton, \$4,993 for Mr. Tryniski, and \$9,140 for Mr. McCullough in 2004; and (d) the expense associated with supplemental retirement plans, amounting to \$362,587 for Mr. Belden, \$98,135 for Mr. Wears, \$55,668 for Mr. Patton, \$8,569 for Mr. Tryniski, and \$352,017 for Mr.

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McCullough in 2004. The Company does not maintain any split-dollar arrangements for the named executive officers.

- (5) Mr. Tryniski joined the Company in June 2003. Mr. McCullough joined the Company in November 2003.

**OPTION/SAR GRANTS IN LAST FISCAL YEAR**

The following table provides further information on grants of stock options pursuant to the 2004 Incentive Plan in fiscal year 2004 to the named executives as reflected in the Summary Compensation Table on page 12.

Name	Options Granted (#)	% of Total Options Granted to Employees in Fiscal Year	Exercise or Base Price (\$/Sh)	Expiration Date	Market Value on Grant Date (\$/Sh)	Potential Realizable Value at Assumed Annual Rates of Stock Price Appreciation for Option Term(\$)	
						5%	10%
Sanford A. Belden	43,158	6.45%	24.15	1/21/14	24.15	655,476	1,661,103
James A. Wears	14,676	2.19%	24.15	1/21/14	24.15	222,896	564,862
Michael A. Patton	14,676	2.19%	24.15	1/21/14	24.15	222,896	564,862
Mark E. Tryniski	14,676	2.19%	24.15	1/21/14	24.15	222,896	564,862
Thomas A. McCullough	0	0%	N/A	N/A			