COMMUNITY BANK SYSTEM INC
Form 424B1
October 03, 2008

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Prospectus

2,200,000 SHARES

COMMUNITY BANK SYSTEM, INC.
Common Stock

We are offering 2,200,000 shares of our common stock. Our common stock is traded on the New York Stock Exchange under the symbol “CBU.” The last reported sale price of our common stock on the New York Stock Exchange on October 2, 2008 was $23.07 per share.

Investing in our common stock involves risks. See “Risk Factors” beginning on page 7.

	PER SHARE	TOTAL
Public offering price	$20.75	$45,650,000
Underwriting discount	$1.14	$2,508,000
Proceeds to us, before expenses	$19.61	$43,142,000

We have granted the underwriters an option to purchase up to an additional 330,000 shares of common stock to cover any over-allotments. The underwriters can exercise this option at any time within thirty days after the offering. The underwriters expect to deliver the shares of common stock to investors on or about October 7, 2008.

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

Shares of our common stock are not deposits or accounts and are not insured or guaranteed by the Federal Deposit Insurance Corporation or any other governmental agency.

Janney Montgomery Scott LLC   Raymond James

FTN Midwest Securities Corp.

The date of this prospectus is October 3, 2008

Community Bank System, Inc.
Market Area

˜ Administrative/Operations Centers
¢ Community Bank, N.A. New York Branches
æ First Liberty Bank & Trust Pennsylvania Branches
Ø Financial Services Locations
¢ RBS Citizens Branches
(to be acquired in pending transaction)

CERTAIN PERSONS PARTICIPATING IN THIS OFFERING MAY ENGAGE IN TRANSACTIONS THAT STABILIZE, MAINTAIN OR OTHERWISE AFFECT THE PRICE OF OUR COMMON STOCK. SPECIFICALLY, THE UNDERWRITERS MAY OVER-ALLOT IN CONNECTION WITH THE OFFERING AND MAY BID FOR, AND PURCHASE, SHARES OF OUR COMMON STOCK IN THE OPEN MARKET AND IMPOSE PENALTY BIDS. FOR A DESCRIPTION OF THESE ACTIVITIES, SEE "UNDERWRITING." SUCH STABILIZING TRANSACTIONS, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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ABOUT THIS PROSPECTUS

You should read this prospectus, together with additional information described under the heading "Where You Can Find More Information."

You should rely only on the information contained or incorporated by reference in this prospectus. We have not, and the underwriters have not, authorized any other person to provide you with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We are not, and the underwriters are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this prospectus and the documents incorporated by reference is accurate only as of each of their respective dates. Our business, financial condition, results of operations and prospects may have changed since those dates.

All references in this prospectus to "Community Bank System," "we," "us," "our" or similar references mean Community Bank System, Inc., and include our consolidated subsidiaries where the context so requires. Currency amounts in this prospectus are stated in U.S. dollars.

WHERE YOU CAN FIND MORE INFORMATION

We are a reporting company and file annual, quarterly and special reports, proxy statements and other information with the Securities and Exchange Commission, or the SEC. You may read and copy such materials at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. You may also obtain copies of such material from the SEC at prescribed rates for the cost of copying by writing to the Public Reference Section of the SEC at the same address. You may call the SEC at 1-800-SEC-0330 for more information on the public reference rooms. You can also find our SEC filings at the SEC's web site at www.sec.gov. You can also inspect reports, proxy statements and other information about us at the offices of the New York Stock Exchange, 11 Wall Street, New York, New York 10005. Our SEC filings can also be found on our website at www.communitybankna.com.

SUMMARY

This summary highlights selected information contained elsewhere, or incorporated by reference, in this prospectus. This summary does not contain all of the information that you should consider before making an investment decision. This prospectus contains forward-looking statements, which involve risks and uncertainties. Our results could differ materially from those anticipated in these forward-looking statements as a result of various factors, including those set forth in “Risk Factors” and elsewhere in this prospectus. You should read the entire prospectus carefully, including the risk factors on page 7 and documents incorporated by reference.

Community Bank System, Inc.

We are a Delaware corporation headquartered in DeWitt, New York, and the parent company of Community Bank, N.A. We are one of the largest community banks headquartered in Upstate New York based on total assets at June 30, 2008. We operate 141 customer facilities and 118 ATMs stretching diagonally from Northern New York to the Southern Tier of New York and west to Lake Erie, as well as in five counties in Northeastern Pennsylvania where we operate as First Liberty Bank & Trust. We were ranked either first or second in deposit market share in 78 of the 112 towns in which we operate, based on publicly available information as of the date of this prospectus. At June 30, 2008, we had approximately $4.7 billion in total assets, $3.2 billion in total deposits, $2.9 billion in total loans and shareholders' equity of $484 million. Community Bank is a member of the Federal Reserve System and the Federal Home Loan Bank System, and its deposits are insured by the Federal Deposit Insurance Corporation, up to applicable limits.

Our business strategy is to operate as a profitable, diversified financial services company providing a variety of banking and other financial services, with an emphasis on consumer and residential mortgage lending and commercial business loans to small and medium-sized businesses. As a result of consolidation of small to medium-sized financial institutions and the deemphasis on retail branch banking by larger bank holding companies in the markets we serve, we believe there is a significant opportunity for a community-focused bank to provide a full range of financial services to small and middle-market commercial and retail customers. Our branches are located in small towns and villages where competition is less intense. We emphasize comprehensive retail and small business products and responsive, decentralized decision-making which reflects our knowledge of our local markets and customers.

Through our subsidiaries, we offer a wide range of commercial and retail banking and financial services to businesses, individuals, agricultural and government customers. Our account services include checking, interest-bearing checking, money market, savings, certificates of deposit and individual retirement accounts. We also offer residential and farm loans, business lines of credit, working capital facilities, inventory and dealer floor plans, as well as installment, commercial, term and student loans. Our lending focuses predominantly on consumer and small to medium-sized business borrowers, which enables our loan portfolio to be highly diversified.

Because we believe that there is a significant potential market for financial services and products, we offer a full range of services to satisfy our customers' financial needs. In addition to traditional banking services and products, we offer personal trust, employee benefit trust, benefits administration and consulting, investment and insurance services to customers in our banking markets as well as in other parts of the country. For the year ended December 31, 2007, our total noninterest income, including income from these financial services and products, was approximately $63.3 million, as compared to $37.9 million for the year ended December 31, 2003.

Consistent with our strategy to increase noninterest income, our wholly owned subsidiary Benefit Plans Administrative Services, Inc. (BPAS) acquired Alliance Benefit Group MidAtlantic (ABG) located in Philadelphia, Pennsylvania in July 2008. In May 2007, BPAS acquired Hand Benefits & Trust, Inc. (HBT) located in Houston, Texas. ABG and HBT provide retirement plan consulting, daily valuation administration, actuarial and ancillary support services.

We have also emphasized expansion of our banking business through business combinations with other banks and the acquisition of assets and deposits. From 2003 through the current date, we have completed seven transactions, which added 28 branches, approximately $800 million in deposits and approximately $710 million in loans.

In addition, we have pending an acquisition with RBS Citizens, National Association (RBS Citizens) to acquire certain assets and liabilities associated with 18 branches in northern New York State with approximately $606 million in deposits and approximately $116 million in loans as of July 31, 2008. We expect to complete this acquisition in the fourth quarter of 2008. At June 30, 2008, after giving pro forma effect to the ABG acquisition, RBS Citizens acquisition and this offering, our total assets would have been approximately $5.3 billion, our total loans would have been approximately $3.0 billion, our total deposits would have been approximately $3.9 billion, and our branch network would have consisted of 159 customer facilities and 134 ATMs.

We are subject to examination and regulation by the Board of Governors of the Federal Reserve System, the Office of the Comptroller of the Currency, or the OCC, and the Federal Deposit Insurance Corporation, or the FDIC. This regulation is intended for the protection of our depositors, not our stockholders.

Our executive offices are located at 5790 Widewaters Parkway, DeWitt, New York 13214, and our phone number is (315) 445-2282. Our web site is located at www.communitybankna.com. The information on our web site is not a part of this prospectus.

Pending Branch Acquisition

On June 24, 2008, we entered into a definitive agreement with RBS Citizens to acquire certain loans and assets, and assume certain deposits, related to 18 RBS Citizens branches located in northern New York State. Under this agreement, we will acquire the facilities and equipment, including 16 ATMs, as well as real estate and leases, associated with the operation of these branches. The transaction is subject to receipt of requisite regulatory approvals and certain other conditions, and is expected to close in the fourth quarter of 2008. We are conducting this offering to raise additional capital to support the RBS Citizens branch acquisition. The consummation of the branch acquisition is not subject to completion of this offering.

We view this acquisition as a unique opportunity to grow our branch network in our existing market areas, as well as to expand our services and market area into contiguous markets in the Northern region of New York State. The acquisition of the RBS Citizens branches provides us the opportunity to increase our business substantially, without a significant increase in corporate administrative overhead costs. Based on total deposits as of June 30, 2007 (the last date for which market share information on deposits is publicly available), we expect the RBS Citizens acquisition to increase our total deposits in the Northern region of New York by $554 million and our deposit market share in that market from 6.4% to 10.4%. In Plattsburgh and surrounding Clinton County (located on the border with Vermont and Canada), the acquisition will increase our deposit market share to a market-leading 22.8% with $292 million in total deposits. We believe that this transaction will provide us with the benefits of acquiring a “whole-bank franchise” in the market area, without the normal whole-bank acquisition costs and risks associated with the integration of senior-level management that come with a whole-bank acquisition.

At July 31, 2008, loans to be acquired under the agreement with RBS Citizens were approximately $116 million and deposits to be assumed were approximately $606 million. Both amounts are subject to adjustments due to run-off or growth of deposits and loans occurring in the ordinary course of business prior to the closing date, and to adjustments in the loan amount based on type of loan and credit quality standards under the agreement.

Recent Developments

Summary of developments since June 30, 2008

Results during the two-month period ended August 31, 2008 reflect similar trends as those experienced during the first six months of 2008. At August 31, 2008 the Company had total assets of $4.75 billion, deposits of $3.25 billion and stockholders' equity of $487 million. Some of the financial highlights for the two-month period ended August 31, 2008 include the following:

- The Company's tax equivalent net interest rate margin remained at the 3.79% level reported for the six months ended June 30, 2008.

- Consistent with historical trends, we experienced seasonally strong loan growth of $65.4 million for the two months ended August 31, 2008, including net growth in all loan types.

- Nonperforming loans declined to $11.2 million or 0.37% of total loans at August 31, 2008, from $11.5 million and 0.39% of total loans at June 30, 2008. At August 31, 2008, the allowance for credit losses represented 1.25% of total loans and 334% of nonperforming loans as compared to 1.27% and 324% as of June 30, 2008, respectively.

- The net market value gain over book value of our available for sale securities portfolio, which contains no FNMA or FHLMC common or preferred stock, increased $2.6 million since June 30, 2008. Based on our analysis, we have determined that any unrealized losses are temporary. We have the ability and intent to hold our investment securities currently in an unrealized loss position to recovery.

- Total deposit balances remained virtually unchanged from June 30, 2008 to August 31, 2008. However, our efforts to better position our funding mix resulted in an additional $45.0 million of growth in core accounts offset by a $45.2 million decline in higher-cost time deposit accounts.

- At August 31, 2008, total borrowings increased $88.5 million, primarily in short-term instruments which were utilized to fund our incremental loan growth as well as an additional $33.7 million of net investment securities purchases.

- All capital ratios of Community Bank, N.A. continue to remain above well-capitalized levels.

The Offering

Issuer	Community Bank System, Inc.
Common stock outstanding before this offering	30,097,809 shares
Common stock offered	2,200,000 shares
Common stock to be outstanding after this offering	32,297,809 shares
Estimated net proceeds to Community Bank System	Approximately $42.9 million
Use of proceeds	To support the acquisition of 18 branches from RBS Citizens. See "Use of Proceeds."
Dividends on common stock	$0.21 per quarter – first and second quarter 2008 $0.22 per quarter – third quarter 2008
New York Stock Exchange symbol	CBU

The number of shares of our common stock to be outstanding after this offering is based on the number of shares outstanding as of October 2, 2008 and excludes the following:

· 2,685,635 shares of common stock issuable upon exercise of outstanding stock options with a weighted average exercise price of approximately $20.34 per share; and

· 2,188,372 shares of common stock reserved for future grants under our stock option plans.

· 330,000 shares subject to the over-allotment option.

Unless otherwise expressly stated or the context otherwise requires, all information in this prospectus assumes the underwriters' over-allotment option will not be exercised. For more information regarding the over-allotment option, see the "Underwriting" section beginning on page 32 of this prospectus.

Risk Factors

Prospective investors should carefully consider the matters set forth under "Risk Factors" beginning on page 7.

Selected Consolidated Financial Data

The table below presents summary consolidated financial information of Community Bank System, Inc. You should read this information together with the information incorporated by reference in this prospectus, including our consolidated financial statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in our Annual Reports on Form 10-K for the years ended December 31, 2007, 2006, 2005, 2004 and 2003 and our Quarterly Report on Form 10-Q for the periods ended June 30, 2008 and 2007. We prepared the summary historical financial data using audited consolidated financial statements for each of the years in the five-year period ended December 31, 2007 and our unaudited financial statements for the six-month periods ended June 30, 2008 and 2007. In the opinion of management, the unaudited interim financial data reflects all adjustments, consisting only of normal and recurring adjustments, necessary for a fair presentation of our results of operations and financial condition for the six months ended June 30, 2008 and 2007. Operating results for the six months ended June 30, 2008 are not necessarily indicative of the results that may be expected for the year ending December 31, 2008. See "Where You Can Find More Information" for a description of how to obtain a copy of the documents incorporated by reference into this prospectus.

We acquired HBT on May 18, 2007, TLNB Financial Corporation, the parent company of Tupper Lake National Bank (TLNB), on June 1, 2007, ONB Corporation, the parent company of Ontario National Bank (ONB), on December 1, 2006, ES&L Bancorp, Inc., the parent company of Elmira Savings and Loan, F.A. (Elmira) on August 11, 2006, one branch from HSBC Bank USA, N.A. on December 3, 2004, First Heritage Bank on May 14, 2004, Grange National Banc Corp. on November 24, 2003, Peoples Bankcorp Inc. on September 5, 2003 and the Upstate New York Global Human Resource Solutions consulting group from PricewaterhouseCoopers on July 31, 2003. Each of these acquisitions was accounted for as a purchase and, accordingly, the results of operations of the acquired businesses are included in the information below since the dates of acquisition.

(In 000's except per share data and ratios)	At or for the Six Months Ended June 30, 2008	2007	At or for the Years Ended December 31, 2007	2006	2005	2004	2003
Income Statement Data:							
Loan interest income	$92,206	$91,025	$186,784	$167,113	$147,608	$137,077	$125,256
Investment interest income	32,015	33,789	69,453	64,788	71,836	75,770	65,915
Interest expense	53,183	58,109	120,263	97,092	75,572	61,752	59,301
Net interest income	71,038	66,705	135,974	134,809	143,872	151,095	131,870
Provision for loan losses	2,350	614	2,004	6,585	8,534	8,750	11,195
Noninterest income	35,037	28,505	63,260	51,679	48,401	44,321	37,887
Gain (loss) on investment securities & early retirement of long-term borrowings	230	(8)	(9,974)	(2,403)	12,195	72	(2,698)
Special charges/acquisition expenses	5	274	382	647	2,943	1,704	498
Noninterest expenses	75,324	67,777	141,692	126,556	124,446	118,195	102,213
Income before income taxes	28,626	26,537	45,182	50,297	68,545	66,839	53,153
Net income	22,185	20,015	42,891	38,377	50,805	50,196	40,380
Diluted earnings per share (1)	$0.74	$0.66	$1.42	$1.26	$1.65	$1.64	$1.49
Diluted earnings per share – cash (1) (3)	$0.83	$0.75	$1.62	$1.47	$1.84	$1.81	$1.64
Balance Sheet Data:							
Investment securities	$1,258,792	$1,219,360	$1,391,872	$1,229,271	$1,303,117	$1,584,633	$1,329,645
Loans	2,922,243	2,767,176	2,821,055	2,701,558	2,411,769	2,358,420	2,128,446
Allowance for loan losses	(37,128)	(36,690)	(36,427)	(36,313)	(32,581)	(31,778)	(29,095)
Intangible assets	253,752	258,110	256,216	246,136	224,878	232,500	196,111
Total assets	4,657,783	4,583,149	4,697,502	4,497,797	4,152,529	4,393,295	3,854,984
Deposits	3,247,348	3,364,577	3,228,464	3,168,299	2,983,507	2,927,524	2,723,950
Borrowings	874,609	704,245	929,328	805,495	653,090	920,511	667,786
Shareholders' equity	$483,648	$459,624	$478,784	$461,528	$457,595	$474,628	$404,828
Capital and Related Ratios:							
Cash dividend declared per share (1)	$0.42	$0.40	$0.82	$0.78	$0.74	$0.68	$0.61
Book value per share (1)	16.16	15.39	16.16	15.37	15.28	15.49	14.29
Tangible book value per share (1)	7.68	6.75	7.51	7.17	7.77	7.90	7.37
Market capitalization (in millions)	617	598	589	690	676	866	694
Tier 1 leverage ratio	7.75%	7.87%	7.77%	8.81%	7.57%	6.94%	7.26%
Total risk based capital to risk adjusted assets	13.48%	14.02%	14.05%	15.47%	13.64%	13.18%	13.01%
Tangible equity to tangible assets	5.22%	4.66%	5.01%	5.07%	5.93%	5.82%	5.70%
Dividend payout ratio	56.5%	60.0%	57.1%	60.7%	43.9%	40.9%	40.2%
Period end common shares outstanding (1)	29,935	29,873	29,635	30,020	29,957	30,642	28,330
Diluted weighted-average shares outstanding (1)	30,154	30,471	30,232	30,392	30,838	30,670	27,035

Selected Performance Ratios:							
Return on average assets	0.96%	0.90%	0.93%	0.90%	1.19%	1.20%	1.16%
Return on average equity	9.18%	8.68%	9.20%	8.36%	10.89%	11.39%	11.78%
Net interest margin	3.79%	3.69%	3.64%	3.91%	4.17%	4.45%	4.68%
Noninterest income/operating income (4)	30.8%	27.7%	26.1%	24.8%	27.7%	21.1%	19.6%
Efficiency ratio(2)	63.4%	63.0%	63.3%	59.9%	56.8%	52.8%	53.4%
Asset Quality Ratios:							
Allowance for loan loss/total loans	1.27%	1.33%	1.29%	1.34%	1.35%	1.35%	1.37%
Nonperforming loans/total loans	0.39%	0.36%	0.32%	0.47%	0.55%	0.55%	0.62%
Allowance for loan loss/nonperforming loans	324%	368%	410%	288%	245%	245%	219%
Net charge-offs/average loans	0.12%	0.07%	0.10%	0.24%	0.33%	0.37%	0.54%
Loan loss provision/net charge-offs	142%	62%	76%	108%	110%	104%	109%

(1) All share and share-based amounts reflect the two-for-one stock split effected as a 100% stock dividend on April 12, 2004.

(2) Efficiency ratio is calculated by dividing operating expenses less amortization of intangibles and special charges/acquisition expenses by noninterest income excluding (loss) gain on investment securities and debt extinguishment and net interest income on a fully taxable equivalent basis.

(3) Cash earnings exclude the after tax effect of the amortization of market value adjustments on net assets acquired in mergers and the amortization of intangible assets. Such earnings are reconciled to GAAP net income in either Table 1 or Table 2 of the applicable Forms 10-Q or 10-K.

(4) Operating income includes noninterest income excluding (loss) gain on investment securities and debt extinguishment and net interest income on a fully taxable equivalent basis.

RISK FACTORS

You should carefully consider the risks described below before investing in our common stock. If any of the following risks actually occur, our business could be harmed. This could cause the price of our stock to decline, and you may lose part or all of your investment. This prospectus contains forward-looking statements that involve risks and uncertainties, including statements about our future plans, objectives, intentions and expectations. Many factors, including those described below, could cause actual results to differ materially from those discussed in forward-looking statements.

Changes in interest rates affect our profitability and assets.

Changes in prevailing interest rates may hurt our business. Although we have diversified our revenue sources, we derive our income mainly from the difference or "spread" between the interest earned on loans, securities and other interest-earning assets, and interest paid on deposits, borrowings and other interest-bearing liabilities. In general, the larger the spread, the more we earn. Interest rates are highly sensitive to many factors that are beyond our control, including general economic conditions and policies of various governmental and regulatory agencies and, in particular, the Federal Reserve. Changes in monetary policy, including changes in interest rates, could influence not only the interest we receive on loans and securities and the amount of interest we pay on deposits and borrowings, but such changes could also affect (1) our ability to originate loans and obtain deposits, which could reduce the amount of fee income generated, (2) the fair value of our financial assets and liabilities and (3) the average duration of our mortgage-backed securities portfolio. If the interest rates paid on deposits and other borrowings increase at a faster rate than the interest rates received on loans and other investments, our net interest income could be adversely affected, which in turn could negatively affect our earnings. Earnings could also be adversely affected if the interest rates received on loans and other investments fall more quickly than the interest rates paid on deposit and other borrowings.

Although management believes it has implemented effective asset and liability management strategies to reduce the potential effects of changes in interest rates on the result of our operations, any substantial, unexpected, prolonged change in market interest rates could have a material adverse effect on our financial condition and results of operations.

Some of our borrowers do not repay their loans, and losses from loan defaults may exceed the reserve we establish for that purpose, which may have an adverse effect on our business.

Some borrowers do not repay loans that we make to them. This risk is inherent in the banking business. If a significant amount of loans were not repaid, it would have an adverse effect on our earnings and overall financial condition. Like all financial institutions, we maintain a reserve for loan losses to provide for loan defaults and nonperformance. The allowance for loan losses reflects our management's best estimate of probable losses in the loan portfolio at the relevant balance sheet date. This evaluation is primarily based upon a review of our and the banking industry's historical loan loss experience, known risks contained in the loan portfolio, composition and growth of the loan portfolio, and economic factors. However, the determination of an appropriate level of loan loss allowance is an inherently difficult process and is based on numerous assumptions. As a result, our reserve for loan losses may not be adequate to cover actual losses, and future provisions for loan losses may adversely affect our earnings.

We depend on the accuracy and completeness of information furnished by others about customers and counterparties.

In deciding whether to extend credit or enter into other transactions, we often rely on information furnished by or on behalf of customers and counterparties, including financial statements, credit reports and other financial information. We may also rely on representations of those customers, counterparties or other third parties, such as independent auditors, as to the accuracy and completeness of that information. Reliance on inaccurate or misleading financial statements, credit reports or other financial information could have a material adverse effect on our business and, in turn, our financial condition and results of operations.

The allowance for loan losses may be insufficient.

Although we try to maintain diversification within our loan portfolio in order to minimize the effect of economic conditions within a particular industry, management also maintains an allowance for loan losses, which is a reserve established through a provision for loan losses charged to expense, to absorb credit losses inherent in the entire loan portfolio. The appropriate level of the allowance is based on management's quarterly analysis of the loan portfolio and represents an amount that management deems adequate to provide for inherent losses, including collective impairment. Among other considerations in establishing the allowance for loan losses, management considers economic conditions reflected within industry segments, and historical losses that are inherent in the loan portfolio. The determination of the appropriate level of the allowance for loan losses inherently involves a high degree of subjectivity and requires management to make significant estimates of current credit risks and future trends, all of which may undergo material changes. Changes in economic conditions affecting borrowers, new information regarding existing loans, identification of additional problem loans and other factors, both within and outside of our control, may require an increase in the allowance for loan losses.

We may fail to implement our acquisitions successfully, achieve savings and realize the other anticipated benefits from the acquisitions because of difficulties in integrating our business operations.

We recently acquired ABG, an employee benefit administration and consulting company based in Philadelphia, Pennsylvania. We have also entered into a definitive agreement to purchase 18 branches in northern New York State from RBS Citizens, which acquisition we expect to complete in the fourth quarter of 2008. The integration of the acquired companies or branches following an acquisition will be complex and time-consuming and will present us with challenges. As a result, we may not be able to operate the combined company as effectively as we expect. We may also fail to achieve the anticipated potential benefits of the acquisitions as quickly or as cost effectively as we anticipate or may not be able to achieve those benefits at all. Specifically, we will face significant challenges integrating the companies' organizations, procedures and operations in a timely and efficient manner and retaining key personnel. In addition, our management will have to dedicate substantial effort to integrating the acquired companies and branches and, therefore, its focus and resources may be diverted from other strategic opportunities and from operational matters. There may also be undisclosed liabilities that we assume with the acquired business.

Regional economic factors may have an adverse impact on our business.

Substantially all of our business is with customers in our market areas in New York and Pennsylvania. Our market areas are generally slow-growing, non-metropolitan cities and towns. Most of our customers are individuals and small and medium- sized businesses which are dependent upon the regional economy. Adverse changes in economic and business conditions in our markets could adversely affect our borrowers, their ability to repay their loans and to borrow additional funds or buy financial services and products from us, and consequently our financial condition and performance.

We face strong competition from other banks and financial institutions, which can hurt our business.

We conduct our banking operations in a number of competitive local markets. In those markets, we compete against commercial banks, savings banks, savings and loans associations, credit unions, mortgage banks, brokerage firms, investment advisory firms, insurance companies and other financial institutions. Many of these entities are larger organizations with significantly greater financial, management and other resources than we have, and they offer the same or similar banking or financial services that we offer in our markets. Moreover, new and existing competitors may expand their business in or into our markets. Increased competition in our markets may result in a reduction in loans, deposits and other sources of our revenues. Ultimately, we may not be able to compete successfully against current and future competitors.

We may face risks with respect to future acquisitions.

Since 2000, we have significantly grown our business through the acquisition of both branches and entire financial institutions. When we attempt to expand our business through mergers or acquisitions, we seek partners that are culturally similar to us, have experienced management and possess either significant market presence or have potential for improved profitability through economies of scale or expanded services. Acquiring other banks, businesses or branches involves various risks commonly associated with acquisitions, including, among other things:

- the time and costs associated with identifying and evaluating potential acquisition and merger partners;
- inaccuracies in the estimates and judgments used to evaluate credit, operations, management and market risks with respect to the target institution;
- our ability to finance an acquisition and possible dilution to our existing stockholders;
- the diversion of our managements' attention to the negotiation of a transaction;
- the incurrence of an impairment of goodwill associated with an acquisition and adverse effects on our results of operations;
- entry into new markets where we lack experience; and
- risks associated with integrating the operations and personnel of the acquired business.

Although we have no current intentions regarding new acquisitions other than the pending acquisition of the RBS Citizens branches, we expect to continue to evaluate attractive acquisition opportunities. Acquisitions typically involve the payment of a premium over book and market values, and, therefore, some dilution of our tangible book value and net income per common share may occur in connection with any future transaction. Furthermore, failure to realize the expected revenue increases, cost savings, increase in geographic or product presence and/or other projected benefits from an acquisition could have a material adverse effect on our financial condition and result of operations.

We depend on dividends from our banking subsidiary for cash revenues, but those dividends are subject to restrictions.

Our ability to satisfy our obligations and pay cash dividends to our stockholders is primarily dependent on the earnings of and dividends from the subsidiary bank. However, payment of dividends by the bank subsidiary is limited by dividend restrictions and capital requirements imposed by bank regulations. As of December 31, 2007, Community Bank, N.A. had the capacity to pay up to $2.5 million in dividends to us without regulatory approval.

Our ability to pay dividends is also subject to our continued payment of interest that we owe on our subordinated junior debentures. As of the date of this prospectus, we have $102 million of subordinated junior debentures outstanding. We have the right to defer payment of interest on the subordinated junior debentures for a period not exceeding 20 quarters although we have not done so to date. If we defer interest payments on the subordinated junior debentures, we will be prohibited, subject to certain exceptions, from paying cash dividends on our common stock until we pay all deferred interest and resume interest payments on the subordinated junior debentures. See "Dividend Policy."

Our proposed branch acquisition will decrease our tangible book value.

In accordance with our agreement with RBS Citizens, we have agreed to pay a premium over the book value of the deposits and loans we will acquire in the RBS Citizens acquisition. This premium will decrease the tangible book value of our common stock in the approximate amount of $1.77 per share to $5.91 per share as of June 30, 2008, on a pro forma basis after giving effect to this offering and the RBS Citizens acquisition. At June 30, 2008, the tangible book value of our common stock was $7.68 per share. While we believe that our common stock trades primarily on the basis of earnings per share and growth in earnings per share, this tangible book value dilution may adversely affect the trading price of our stock as our stock may trade, in part, on the basis of our tangible book value per share.

We may be required to record impairment charges in respect of our goodwill, other intangible assets and investment portfolio.

As of June 30, 2008, we had approximately $253.8 million in intangible assets including $234.7 million in goodwill and $1.1 billion in available-for-sale investment securities. In the event our intangible assets are determined to be impaired, we will be required to record a charge against income. We may also be required to record impairment charges on our investment securities if they suffer a decline in value that is considered other-than-temporary. We test our goodwill and intangible assets for impairment at least annually and more frequently when events or circumstances indicate that impairment may have occurred. Numerous factors, including lack of liquidity for resales of certain investment securities, absence of reliable pricing information for investment securities, adverse changes in the business climate, adverse actions by regulators, unanticipated changes in the competitive environment or a decision to change our operations or dispose of an operating unit could have a negative effect on our investment portfolio, goodwill or other intangible assets in future periods. If an impairment charge is significant enough to result in negative net income for the period, it could affect the ability of our bank subsidiary to upstream dividends to us, which could have a material adverse effect on our liquidity and our ability to pay dividends to stockholders and could also negatively impact our regulatory capital ratios and result in us not being classified as "well capitalized" for regulatory purposes.

Our indirect automobile lending program involves credit risks.

A significant portion of our lending involves the purchase of consumer automobile sales contracts from new and used automobile dealers primarily located in Upstate New York and Northeastern Pennsylvania. As of June 30, 2008, we had approximately $470.8 million of indirect loans outstanding. While these loans have higher yields than many of our other lending products, they involve significant risks in addition to normal credit risk. Potential risk elements associated with indirect lending include, among other risks present in all lending, difficulty in monitoring the collateral, and limited personal contact with the borrower as the result of indirect lending through dealers. While our indirect automobile loans are secured, they are secured by depreciating assets and characterized by loan to value ratios that could result in our not recovering the full value of an outstanding loan on repossession of the automobile.

Diversification in types of financial services may adversely affect our financial performance.

As part of our business strategy, we may further diversify our lines of business into areas that are not traditionally associated with the banking business. As a result, we would need to manage the development of new business lines in which we have not previously participated. Each new business line would require the investment of additional capital and the significant involvement of our senior management to develop and integrate the service subsidiaries with our traditional banking operations. We can offer no assurances that we will be able to develop and integrate new services without adversely affecting our financial performance.

As a result of our diversification, we have grown more reliant on non-interest income for profitability. Our diversification efforts have focused on financial services businesses that generally provide steady fee and commission income but do not generate the interest-earning assets that contribute to net interest income. In the event the fee income from our non-bank businesses should decline, our continued profitability may depend on our ability to reduce non-interest expense to a level that our revenue can support or to find other non-interest revenue streams to replace that income.

We may be adversely affected by changes in banking laws, regulations, and regulatory practices. Such changes would affect our ability to offer new products and services, obtain financing, receive dividends from our bank subsidiary, attract deposits, or make loans at satisfactory spreads. Such changes may also result in the imposition of additional costs.

The banking industry is heavily regulated, and such regulations are intended primarily for the protection of depositors and the federal deposit insurance funds, not shareholders or holders of subordinated debt. As a bank holding company, we are subject to regulation by the Federal Reserve Board and our bank subsidiary is subject to regulation by the OCC. These regulations affect lending practices, capital structure, investment practices, dividend policy and growth. In addition, we have non-bank operating subsidiaries from which we derive income. Certain of these non-bank subsidiaries engage in providing investment management and insurance brokerage services, which industries are also heavily regulated on both a state and federal level. In addition, changes in laws, regulations and regulatory practices affecting the financial services industry could subject us to additional costs, limit the types of financial services and products we may offer and/or increase the ability of non-banks to offer competing financial services and products, among other things. Failure to comply with laws, regulations or policies could result in sanctions by regulatory agencies, civil money penalties and/or reputation damage, which could have a material adverse effect on our business, financial condition and results of operations. While we have policies and procedures designed to prevent any such violations, there can be no assurance that such violations will not occur.

The market price and trading volume of our common stock may be volatile.

The trading volume in our common stock may fluctuate and cause significant price variations to occur. Recently, the stock market generally has experienced extreme price and volume fluctuations, and general economic and political conditions and industry factors, such as economic slowdowns and recessions, interest rate changes or credit loss trends, could also cause our stock price to decrease regardless of operating results. If the market price of our common stock declines significantly, you may be unable to resell your shares at or above the public offering price. We cannot assure you that the market price of our common stock will not fluctuate or decline significantly in the future.

FORWARD-LOOKING STATEMENTS

This document contains or incorporates by reference a number of forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934 regarding our financial condition, results of operations, earnings outlook and business prospects. You can find many of these statements by looking for words such as “will,” “may,” “should,” “expects,” “projects,” “anticipates,” “believes,” “intends,” “e “strategy,” “plan,” “potential,” “possible” and other similar expressions.

The forward-looking statements involve certain risks and uncertainties. We cannot predict the results or actual effects of our plans and strategies, which are inherently uncertain. Accordingly, actual results may differ materially from those expressed in, or implied by, the forward-looking statements. Some of the factors that may cause our actual results or earnings to differ materially from those contemplated by the forward-looking statements include, but are not limited to, those discussed under “Risk Factors” and those discussed in our SEC filings that are incorporated herein by reference, including future filings.

Because these forward-looking statements are subject to assumptions and uncertainties, actual results may differ materially from those expressed or implied by these forward-looking statements. You are cautioned not to place undue reliance on these statements, which speak only as of the date of this document or the date of any document incorporated by reference in this document. Except to the extent required by applicable law or regulation, we undertake no obligation to update these forward-looking statements to reflect events or circumstances after the date of this document or to reflect the occurrence of unanticipated events.

You should refer to our periodic and current reports filed with the SEC (and incorporated by reference herein) for further information on other factors that could cause actual results to be significantly different from those expressed or implied by these forward-looking statements. See above under the caption “Where You Can Find More Information” in this prospectus.

USE OF PROCEEDS

We estimate that the net proceeds from the sale of the 2,200,000 shares of common stock that we are offering at the public offering price of $20.75 per share will be approximately $42.9 million after deducting underwriting discounts and commissions and estimated offering expenses payable by us. If the underwriters exercise their over-allotment option in full, we estimate that our net proceeds from this offering will be approximately $49.4 million.

The purpose of this offering is to raise additional capital to support the RBS Citizens branch acquisition and to enable us to remain in the highest category of capital adequacy for federal bank regulatory purposes. We expect to contribute the net proceeds of this offering to Community Bank to be used for these purposes.

PRICE RANGE OF OUR COMMON STOCK AND DIVIDEND INFORMATION

Our common stock is traded on the New York Stock Exchange under the symbol CBU. The following table sets forth for the periods indicated the high and low sale prices for our common stock, as reported on the New York Stock Exchange, and the dividends declared per share on our common stock.

	High	Low	Cash Dividends Declared Per Share
Year Ending December 31, 2008			
Fourth Quarter (through October 2, 2008)	$25.98	$22.55	$ -
Third Quarter	33.00	19.52	0.22
Second Quarter	26.88	20.50	0.21
First Quarter	26.45	17.91	0.21
Year Ended December 31, 2007			
Fourth Quarter	$21.85	$17.70	$0.21
Third Quarter	21.69	16.61	0.21
Second Quarter	21.38	19.63	0.20
First Quarter	23.63	19.64	0.20
Year Ended December 31, 2006			
Fourth Quarter	$25.11	$21.79	$0.20
Third Quarter	22.84	19.45	0.20
Second Quarter	22.38	18.75	0.19
First Quarter	24.31	20.64	0.19

On October 2, 2008, the last reported sale price of our common stock on the New York Stock Exchange was $23.07. As of October 2, 2008, there were 30,097,809 shares of our common stock outstanding, held by approximately 3,530 holders of record.

DIVIDEND POLICY

We have historically paid regular quarterly cash dividends on our common stock, and our board of directors presently intends to continue the payment of regular quarterly cash dividends, subject to the need for those funds for debt service and other purposes. However, because substantially all of the funds available for the payment of dividends are derived from Community Bank, future dividends will depend upon the earnings of Community Bank, its financial condition and its need for funds.

Moreover, there are a number of federal banking policies and regulations that would restrict our ability to pay dividends. In particular, because Community Bank is a depository institution whose deposits are insured by the FDIC, it may not pay dividends or distribute capital assets if it is in default on any assessment due the FDIC. Also, as a national bank, Community Bank is subject to OCC regulations which impose certain minimum capital requirements that would affect the amount of cash available for distribution to us. Lastly, under Federal Reserve policy, we are required to maintain adequate regulatory capital, are expected to serve as a source of financial strength to Community Bank and to commit resources to support Community Bank. These policies and regulations may have the effect of reducing the amount of dividends that we can declare to our stockholders.

CAPITALIZATION

The following table provides (i) our capitalization as of June 30, 2008, (ii) our capitalization as adjusted to give effect to this offering, (iii) our capitalization on a pro forma basis to give effect to the proposed acquisition of 18 bank branches from RBS Citizens and the ABG acquisition, and (iv) our actual and pro forma capital ratios.

	As of June 30, 2008		
		As Adjusted	
	CBSI Historical	Common Stock Offering (1)	Common Stock Offering and Acquisitions (2)
	(Dollars in Thousands)		
Company obligated mandatorily redeemable preferred securities of subsidiary holding solely junior subordinated debentures of the Company	$101,963	$101,963	$101,963
SHAREHOLDERS' EQUITY			
Common stock, $1.00 par value; 50,000,000 shares authorized; 33,299,520 shares outstanding (historical)	33,300	35,500	35,500
Additional paid-in capital	213,970	254,649	254,649
Retained earnings	319,927	319,927	319,927
Accumulated other comprehensive loss	(9,921)	(9,921)	(9,921)
Treasury stock, at cost (3,364,811 shares)	(73,628)	(73,628)	(73,628)
Total Shareholders' Equity	483,648	526,527	526,527
Total Capitalization	$585,611	$628,490	$628,490
COMPANY CAPITAL RATIOS (3):			
Tier 1 risk-based capital ratio	11.98%	13.49%	10.23 %
Total risk-based capital ratio	13.23%	14.74%	11.48 %
Leverage ratio	7.75%	8.73%	6.05 %

(1) Assumes the sale of approximately 2,200,000 shares issued at a price of $20.75 per share less underwriting discounts and commissions of approximately $2.5 million and estimated expenses related to the offering of approximately $0.3 million.

(2) Reflects the sale of common stock and consummation of the ABG acquisition and the RBS Citizens branch acquisition.

(3) The capital ratios, as adjusted, are computed including the total estimated net proceeds from the sale of the common stock, in a manner consistent with regulatory guidelines.

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PRO FORMA CONSOLIDATED STATEMENT OF FINANCIAL CONDITION
June 30, 2008

The table below contains our unaudited pro forma consolidated financial condition, assuming that this offering and the acquisitions of ABG and the RBS Citizens branches were all completed on June 30, 2008. The information contained in the table should be read in conjunction with the audited financial statements and notes included in our Annual Report on Form 10-K for the year ended December 31, 2007, and the unaudited financial statements and notes included in our Quarterly Report on Form 10-Q for the quarter ended June 30, 2008, which are incorporated by reference in this prospectus. This information has been prepared by us, is unaudited and may not be indicative of actual results.

(Dollars in Thousands)	CBSI Historical	ABG acquisition (1)	Common Stock Offering (2)	RBS Citizens Branch Acquisition (3) (4)	CBSI Pro Forma
ASSETS					
Cash and cash equivalents	$123,233		$42,879	$410,783	$576,895
Investment securities	1,258,792	(5,079)			1,253,713
Loans	2,922,243			115,843	3,038,086
Allowance for loan losses	(37,128)			(1,471)	(38,599)
Premises and equipment, net	69,556	57		2,730	72,343
Intangible assets, net	253,752	4,974		77,904	336,630
Other assets	67,335	500		291	68,126
TOTAL ASSETS	$4,657,783	$452	$42,879	$606,080	$5,307,194
LIABILITIES AND SHAREHOLDERS' EQUITY					
Liabilities:					
Deposits:					
Noninterest bearing	$584,752			$97,058	$681,810
Interest bearing	2,662,596			508,582	3,171,178
Total Deposits	3,247,348			605,640	3,852,988
Borrowings	772,646				772,646
Subordinated debt held by unconsolidated subsidiary trusts	101,963				101,963
Accrued interest and other liabilities	52,178	452		440	53,070
TOTAL LIABILITIES	4,174,135	452		606,080	4,780,667

Shareholders' equity					
Common stock	33,300		2,200		35,500
Additional paid-in capital	213,970		40,679		254,649
Retained earnings	319,927				319,927
Accumulated other comprehensive loss	(9,921)				(9,921)
Treasury stock	(73,628)				(73,628)
TOTAL SHAREHOLDERS' EQUITY	483,648		42,879		526,527
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$4,657,783	$452	$42,879	$606,080	$5,307,194

(1) Reflects July 2008 acquisition of ABG, a provider of retirement plan administration and consulting services.

(2) Assumes the sale of approximately 2,200,000 shares issued at a price of $20.75 per share less underwriting discounts and commissions of approximately $2.5 million and estimated expenses related to the offering of approximately $0.3 million.

(3) Reflects RBS Citizens branch acquisition, including $77.9 million excess of purchase price over the fair value of net assets acquired. All information is as of July 31, 2008. With the additional funds available from the securities offerings and from the net deposits assumed in the RBS Citizens branch acquisition, we intend to increase the amount of investment securities held by approximately $411 million, which will correspondingly reduce cash by approximately $411 million.

(4) The actual amounts of loans to be acquired, and deposits to be assumed, under the agreement with RBS Citizens are subject to certain adjustments contemplated by the agreement. As of July 31, 2008, RBS Citizens loans to be acquired by us were approximately $116 million and RBS Citizens deposits to be assumed by us were approximately $606 million. As a result of the additional intangible asset created by the RBS Citizens acquisition, pro forma tangible book value per share will decrease to $5.91 from $7.68 as of June 30, 2008.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RECENT RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements incorporated by reference in this prospectus. This discussion contains forward-looking statements, which involve risks and uncertainties. Our actual results could differ materially from those anticipated in the forward-looking statements as a result of certain factors, including but not limited to those discussed in "Risk Factors" and elsewhere in this prospectus. The May 18, 2007 acquisition of HBT and the June 1, 2007 acquisition of TLNB have been accounted for as purchases. Accordingly, the results of operations of HBT and TLNB are included in the information below since the date of acquisition.

Net Income and Profitability

As shown in Table 1, diluted earnings per share for the second quarter and June year-to-date of $0.37 and $0.74, respectively, were $0.03 and $0.08 higher than the diluted earnings per share generated in the same periods of last year. Net income for the quarter of $11.3 million was up 9.0% over the second quarter of 2007 and net income of $22.2 million for the first six months of 2008 increased 10.8% from the amount earned in the first half of 2007. As compared to the first quarter of 2008, net income increased $0.4 million or 3.6% and diluted earnings per share increased $0.01 or 2.8%.

Second quarter net interest income of $35.4 million was up $2.1 million or 6.3% from the comparable prior year period, and net interest income for the first six months of 2008 increased $4.3 million or 6.5% over the first half of 2007. The current quarter's provision for loan losses increased $1.2 million as compared to the second quarter of 2007 and increased $1.7 million for the first six months of 2008 as compared to the same period of 2007, reflective of organic loan growth in the quarter. Second quarter noninterest income, excluding securities gains and losses, was $17.7 million, up $2.7 million or 18% from the second quarter of 2007, while YTD noninterest income of $35.0 million increased $6.5 million or 23% from the prior year level. Operating expenses of $37.0 million for the quarter and $75.3 million for the first six months of 2008 were up $2.8 million or 8.3% and $7.3 million or 10.7% respectively, from the comparable prior year periods. A significant portion of the increase was attributable to the acquisitions of TLNB and HBT during the second quarter of 2007.

In addition to the earnings results presented above in accordance with generally accepted accounting principles (GAAP), Community Bank System provides cash earnings per share, which excludes the after-tax effect of the amortization of intangible assets and acquisition-related market value adjustments. Management believes that this information helps investors better understand the impact of acquisition activity on reported results. Cash earnings per share for the second quarter and the first six months of 2008 were $0.42 and $0.83, respectively, up 7.7% and 10.7% from the $0.39 and $0.75 earned in the comparable periods of 2007.

As reflected in Table 1, the primary reasons for improved earnings over the prior year were higher noninterest income and net interest income, partially offset by higher operating expenses and loan loss provision. Net interest income for the second quarter and year-to-date period increased as compared to the comparable periods of 2007 as a result of higher net interest margins as well as acquired and organic loan growth. Excluding security gains and losses, noninterest income increased due to a strong performance by our employee benefits consulting and plan administration business, as a result of significant organic growth and the acquisition of HBT, as well as higher banking service fees, including account fees and debit card related revenues. An increase in total loans and higher net charge-offs were the primary reasons for the increase in the loan loss provision. Operating expenses increased for the quarter and year-to-date periods, primarily due to costs associated with the two acquisitions in the last year, as well as higher business development and volume-based processing costs, increased facility-based utilities and maintenance costs, and higher personnel expenses. As compared to the first quarter of 2008, operating expenses decreased $1.4 million or 3.7%, reflective of seasonally lower occupancy, professional and personnel-related costs.

A condensed income statement and a reconciliation of GAAP-based earnings results to cash-based earnings results are as follows:

Table 1: Summary Income Statements

	Three Months Ended June 30,		Six Months Ended June 30,	
(000's omitted, except per share data)	2008	2007	2008	2007
Net interest income	$35,440	$33,338	$71,038	$66,705
Provision for loan losses	1,570	414	2,350	614