

Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

COMMUNITY BANK SYSTEM INC  
Form 11-K  
June 29, 2004

United States  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 11-K

(Mark One)

ANNUAL REPORT PURSUANT TO SECTION 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934 (FEE REQUIRED)

For the fiscal year ended December 31, 2003 or

TRANSACTION REPORT PURSUANT TO SECTION 15 (d) OF THE SECURITIES AND EXCHANGE ACT OF 1934 (NO FEE REQUIRED)

For the transaction period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-11716

A. Full title of the plan and the address of the plan, if different from that of the issuer named below:

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
5790 Widewaters Parkway  
DeWitt, New York 13214

B. Name of Issuer of the securities held pursuant to the plan and the address of its principal executive office.

Community Bank System, Inc.  
5790 Widewaters Parkway  
DeWitt, New York 13214

REQUIRED INFORMATION

1. Not applicable
2. Not applicable
3. Not applicable
4. The Community Bank System, Inc. 401(k) Employee Stock Ownership Plan (the "Plan") is subject to the requirements of the Employee Retirement Income Security Act of 1974 ("ERISA"). Attached hereto as Appendix I is a copy of the most recent financial statements of the Plan prepared in accordance with the financial reporting requirements of ERISA.

Exhibits

(23) Consent of PricewaterhouseCoopers LLP.

Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

Signatures

Pursuant to the requirements of the Securities Exchange Act of 1934, the trustee has duly caused this annual report to be signed on its behalf by the undersigned, thereunto duly authorized.

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan

Community Bank, N. A., Trustee

Dated: June 25, 2004

/s/ Mark E. Tryniski

-----  
Mark E. Tryniski  
Treasurer, Chief Operating Officer and  
Chief Financial Officer

Appendix I

Financial Statements

Community Bank System, Inc. 401(k) Employee Stock Ownership Plan

December 31, 2003 and 2002

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002  
-----

	Page (s)
Report of Independent Auditors .....	1
Financial Statements	
Statements of Net Assets Available for Benefits, .....	2
Statements of Changes in Net Assets Available for Benefits, .....	3
Notes to Financial Statements .....	4 -8
Supplemental Schedule	
Schedule of Assets (Held at End of Year) (Schedule H, Part IV, Item (i)) ....	9

Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

Note: All other schedules are omitted since they are not applicable or are not required based on the disclosure requirements of the Employee Retirement Income Security Act of 1974 and applicable regulations issued by the Department of Labor.

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

-----

Report of Independent Registered Public Accounting Firm

Compensation Committee and Participants of  
Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan

In our opinion, the accompanying statements of net assets available for benefits and the related statements of changes in net assets available for benefits present fairly, in all material respects, the net assets available for benefits of Community Bank System, Inc. 401(k) Employee Stock Ownership Plan (formerly the Community Bank System, Inc. Employee Savings and Retirement Plan) (the "Plan") at December 31, 2003 and 2002, and the changes in net assets available for benefits for the years ended December 31, 2003 and 2002 in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Plan's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States) and auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

Our audits were conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The supplemental schedule of assets held for investment purposes is presented for the purpose of additional analysis and is not a required part of the basic financial statements but is supplementary information required by the Department of Labor's Rules and Regulations for Reporting and Disclosure under the Employee Retirement Income Security Act of 1974. This supplemental schedule is the responsibility of the Plan's management. The supplemental schedule has been subjected to the auditing procedures applied in the audits of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

/s/ PricewaterhouseCoopers LLP

Syracuse, New York  
May 28, 2004

Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

1

Community Bank System, Inc.  
 401(k) Employee Stock Ownership Plan  
 (formerly the Community Bank System, Inc.  
 Employee Savings and Retirement Plan)  
 Notes to Financial Statements  
 December 31, 2003 and 2002

	2003	2002
-----		
Assets		
Investments at fair value		
Mutual funds	\$ 27,105,195	\$ 21,053,219
Common stock of Plan sponsor	16,552,974	10,605,978
Self directed brokerage	231,668	125,406
Loans to participants	1,336,423	1,057,551
	-----	-----
Total investments	45,226,260	32,842,154
Receivable from plan merger (Note F)	3,391,468	--
Contributions receivable - employee	81,547	--
Contributions receivable - employer	584,348	459,406
	-----	-----
Net assets available for benefits	\$ 49,283,623	\$ 33,301,560
	=====	=====

The accompany notes are an integral part of the financial statements.

2

Community Bank System, Inc.  
 401(k) Employee Stock Ownership Plan  
 (formerly the Community Bank System, Inc.  
 Employee Savings and Retirement Plan)  
 Notes to Financial Statements  
 December 31, 2003 and 2002

	2003	2002
-----		
Additions		
Employee contributions	\$ 2,871,482	\$ 3,158,388
Employer contributions	1,321,959	1,162,120
Interest income	138,073	18,818
Dividend income	1,115,367	1,044,084
Net appreciation (depreciation) in the fair value of investments	9,246,282	(767,771)
Transfer from merged plan (Note F)	3,391,468	--
	-----	-----
	18,084,631	4,615,639
	-----	-----
Deductions		
Benefits paid to participants	2,026,077	1,143,335
Administrative expenses	76,491	73,338
	-----	-----
	2,102,568	1,216,673
	-----	-----
Net increase in plan assets	15,982,063	3,398,966

## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

Net assets available for benefits		
Beginning of year	33,301,560	29,902,594
	-----	-----
End of year	\$ 49,283,623	\$ 33,301,560
	=====	=====

The accompany notes are an integral part of the financial statements.

3

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

---

### A. Description of the Plan

The following description of the Community Bank System, Inc. 401(k) Employee Stock Ownership Plan (formerly the Community Bank System, Inc. Employee Savings and Retirement Plan) ("the Plan") provides only general information. Participants should refer to the Plan agreement for a more complete description of the Plan's provisions.

#### General

The Plan is a defined contribution plan which covers substantially all Community Bank System, Inc. (the "Company") employees who are age eighteen or older. Employees must have 1 year of service to be eligible for the Company's contribution. The Plan also qualifies as an employee stock ownership plan under the meaning of Section 4975(e)(7) of the Internal Revenue Code. The Plan is subject to the provisions of the Employment Retirement Income Security Act of 1974 (ERISA).

#### Contributions

Participants may make voluntary contributions of up to 90% of their total compensation on a pre-tax or after-tax basis up to a maximum contribution of \$12,000. Voluntary cash contributions of up to 6% of total eligible compensation are matched 50% by the Company and such match was \$765,430 and \$702,714 in 2003 and 2002, respectively. Within certain maximum limitations, the amount of the Company's annual discretionary contributions are determined by the Board of Directors. In addition, the Company may make discretionary profit sharing contributions to the Plan which are allocated to individual participant accounts. Such voluntary contributions were \$556,529 and \$459,406 in 2003 and 2002, respectively.

#### Participant Accounts

Each participant's account is credited with the participant's contribution and allocations of (a) the Company's contribution and (b) Plan earnings, and charged with an allocation of administrative expenses. Allocation of Plan earnings and administrative expenses are based on participant earnings or account balances, as defined. The benefit to which a participant is entitled is the benefit that can be provided from the participant's vested account. Forfeited accounts are allocated annually to eligible participant accounts based on the ratio of each eligible

## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

participant's compensation to total eligible participant compensation. Forfeited accounts allocated to eligible participants amounted to \$8,980 and \$9,087 for 2003 and 2002, respectively.

### Vesting

Participants are immediately vested in their contributions and the Company's discretionary profit sharing contributions. Vesting in the Company's matching contribution portion plus actual earnings thereon is based on years of continuous service. A participant is 100 percent vested after three years of service.

### Participant Loans

Participants may borrow from the Plan a minimum of \$1,000 up to a maximum equal to the lesser of \$50,000 or 50 percent of their vested account balance. Loans are collateralized by the balance in the participant's account and bear interest at a rate of prime plus two percent.

4

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

---

### Payment of Benefits

Normal retirement date for participants under the Plan is the later of age 65 or the completion of 5 years of service. Upon termination of service due to death, disability or retirement, the participant will receive either a lump sum amount or installment payments equal to the value of the participant's vested interest in his or her account. If some or all of a participant's account balance is allocated to the employee stock option feature of the Plan, that portion of the Plan benefit may be paid in the form of Company stock. Upon termination of employment, if the account balance is less than \$5,000, the participant will receive a single lump sum amount equal to the value of his or her account, otherwise, the participant may elect to defer payment up to age 65. Hardship withdrawals of up to 100% of employee contributions are available if Internal Revenue Service guidelines are met.

### Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Plan to discontinue contributions at any time and terminate the Plan subject to the terms of ERISA. In the event of a termination of the Plan, the net assets of the Plan are to be set aside for participating employees based upon balances then credited to individual accounts. Participants shall be vested 100% in the assets so allocated to their accounts.

## B. Significant Accounting Policies

### Basis of Accounting

The financial statements included herein have been prepared on an accrual

## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

basis of accounting in accordance with accounting principles generally accepted in the United States of America.

### Investments

Investments are stated at aggregate fair value, except for the SEI Stable Asset GIC Fund which is stated at cost, which approximates fair value. Securities which are traded on a national securities exchange are valued at the last reported sales price on the last business day of the Plan year. Participant loan receivable balances are reported at cost, which approximates fair value.

The Plan presents in the statement of changes in net assets, the net appreciation (depreciation) in the fair value of its investments which consists of realized gains or losses and unrealized appreciation (depreciation) on those investments.

Purchases and sales of securities are recorded on the trade date. Gains or losses on sales of securities are based on average cost. Interest income is recorded on the accrual basis. Dividends are recorded on the ex-dividend date.

### Payment of Benefits

Benefits are recorded when paid.

### Administrative Expenses

Certain administrative expenses are paid by the Company. These amounted to approximately \$173,000 and \$141,000, including approximately \$136,000 and \$104,000 paid to Benefit Plans Administrative Services ("BPA"), in 2003 and 2002, respectively. (See Note D).

5

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

---

### Inactive Accounts

Account balances of individuals who have withdrawn from participation in the Plan were on an accumulated basis of approximately \$7,949,961 and \$5,540,627 at December 31, 2003 and 2002, respectively.

### Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### Risks and Uncertainties

## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

The plan provides for various investment options in mutual funds and Company stock. Investment securities are exposed to various risks, such as interest rate, market and credit. Due to the level of risk associated with certain investment securities and the level of uncertainty related to changes in the value of investment securities, it is at least reasonably possible that changes in risk in the near term would materially affect participants' account balances and the amounts reported in the statement of net assets available for plan benefits and the statement of changes in net assets available for plan benefits.

### C. Investments

Investments are held within various common funds maintained by the Community Bank, N.A. Trust Department. Participants, at their discretion, may allocate contributions and account balances between various investment options offered by the Plan. A brief description of these investment options, as provided by the plan administrator, follows:

Community Bank System, Inc. Employee Stock Ownership Fund - these Funds invest in the common stock of the Plan sponsor, which is traded on the New York Stock Exchange under the symbol "CBU".

SEI Stable Asset GIC Fund - a mutual fund that holds primarily a diversified portfolio of stable value contracts issued by insurance companies and banks. Investments in the SEI Stable Asset GIC Fund are not marketable securities and are reported at cost, which approximates fair value.

Washington Mutual Investors Fund - a mutual fund that invests in common stocks and securities convertible into such common stocks.

Federated Total Return Bond Fund - a mutual fund seeking to provide total return by investing primarily in a diversified portfolio of investment grade fixed income securities.

Manager Special Equity Fund - a mutual fund that invests in equity securities of small- and medium-sized U.S. companies.

6

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

---

Massachusetts Investors Growth Fund - a mutual fund that invests in common stocks and securities convertible into common stocks that offer long-term growth.

EuroPacific Growth Fund - a mutual fund that invests in stocks of issuers located in Europe and the Pacific Basin.

Dreyfus S&P 500 Index Fund - a mutual fund that invests in equities and seeks to match the performance of the S&P 500 Composite Stock Price Index.

Federated Mid-Cap Index Fund - a mutual fund primarily that invests in



## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

stocks of U.S. companies.

TD Waterhouse IDA Account - participants select the individual investment securities, including equity securities, mutual funds, and bonds.

The fair value of individual investments which represent 5% or more of net assets available for benefits at either December 31, 2003 or 2002 are as follows:

	2003	2002
Community Bank System, Inc. Common Stock	\$ 16,552,974	\$ 10,605,978
SEI Stable Asset GIC Fund	9,011,419	8,095,573
Washington Mutual Investors Fund	7,130,530	5,418,673
Federated Total Return Bond Fund	2,843,347	2,743,170
Manager Special Equity Fund	2,586,283	1,389,311

The Plan's investments appreciated/(depreciated) in value as follows:

	2003	2002
Mutual Funds	\$ 2,996,506	\$ (1,840,959)
Common Stock of Plan Sponsor	6,249,776	1,073,188
	-----	-----
Total net depreciation in fair value of investments	9,246,282	\$ (767,771)
	=====	=====

#### D. Transactions with Parties-in-Interest

The assets of the Plan are managed by BPA, a subsidiary of Community Bank System, Inc. The Company paid BPA approximately \$136,000 and \$104,000 for record keeping, trustee and other services in 2003 and 2002, respectively.

7

Community Bank System, Inc.  
 401(k) Employee Stock Ownership Plan  
 (formerly the Community Bank System, Inc.  
 Employee Savings and Retirement Plan)  
 Notes to Financial Statements  
 December 31, 2003 and 2002

---

The Plan held 675,632 and 676,616 shares of the sponsor company common stock at December 31, 2003 and 2002, respectively. The cost of these shares at December 31, 2003 and 2002 is \$6,814,388 and \$5,915,539, respectively, and their fair value at December 31, 2003 and 2002 is \$16,552,974 and \$10,605,978, respectively. On January 21, 2004, the Company announced a two-for-one stock split to be effected in the form of a 100% stock dividend paid on April 12, 2004 to shareholders of record on March 17, 2004. Accordingly, all share amounts have been adjusted to reflect the stock split.

Dividends received on the investment in Community Bank System, Inc. common stock amounted to \$413,814 and \$349,520 for the years ended December 31, 2003 and 2002, respectively. The Plan sold 602,196 and 89,348 shares of

## Edgar Filing: COMMUNITY BANK SYSTEM INC - Form 11-K

Community Bank System, Inc. common stock during 2003 and 2002, respectively, and purchased 608,478 and 105,870 shares of Community Bank System, Inc. common stock during 2003 and 2002, respectively.

### E. Income Tax Status

The Plan obtained its most recent determination letter in July 2003, in which the Internal Revenue Service stated that the plan, as then designed, was in compliance with Section 401(a) of the Internal Revenue Code. The Plan has been amended since receiving the determination letter, however, the Plan administrator believes that the Plan is currently designed and being operated in compliance with the applicable requirements of the Internal Revenue Code.

### F. Plan Merger

On November 24, 2003, the Company acquired Grange National Banc Corp. Effective December 30, 2003, the Grange National Banc Corp. Employee Stock Ownership Plan with 401(k) provisions was merged into the Plan. Accordingly, total plan assets of \$3,391,468 were transferred to the Plan in 2004.

8

Community Bank System, Inc.  
401(k) Employee Stock Ownership Plan  
(formerly the Community Bank System, Inc.  
Employee Savings and Retirement Plan)  
Notes to Financial Statements  
December 31, 2003 and 2002

(a)	(b) Identify of issue, borrower, lessor or similar party	(c) Description of investment including maturity date, rate of interest, collateral, par or maturity value	(e) Current value
	Mutual Funds		
	SEI Stable Asset GIC Fund	Mutual Fund - 9,011,419 shares	\$ 9,011,419
	Washington Mutual Investors Fund	Mutual Fund - 247,760 shares	7,130,530
	Federated Total Return Bond Fund	Mutual Fund - 262,301 shares	2,843,347
	Manager Special Equity Fund	Mutual Fund - 32,950 shares	2,586,283
	Massachusetts Investors Growth Fund	Mutual Fund - 163,758 shares	1,853,740
	EuroPacific Growth Fund	Mutual Fund - 55,794 shares	1,685,537
	Dreyfus S&P 500 Index Fund	Mutual Fund - 44,561 shares	1,445,117
	Federated Mid-Cap Index Fund	Mutual Fund - 28,937 shares	549,222
			-----
			27,105,195
	Common stock of plan sponsor		
*	Community Bank Systems, Inc.	Common stock - 675,632 shares	16,552,974
	Self directed brokerage		231,668
	TD Waterhouse IDA Accounts	Self-directed brokerage	231,668
	Loan Fund		
	Participants loans	5% - 10-1/2%	1,336,423
			-----
	Total investments		\$ 45,226,260 =====

\* Denotes party-in-interest