

COMMUNITY BANK SYSTEM, INC.  
Form DEF 14A  
March 29, 2018

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

SCHEDULE 14A  
Proxy Statement Pursuant to Section 14(a) of the  
Securities Exchange Act of 1934  
(Amendment No. )

Filed 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.

(Name of Registrant as Specified in Its Charter)

(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:

(2)

Aggregate number of securities to which transaction applies:

(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):

(4)

Proposed maximum aggregate value of transaction:

(5)

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Fee paid previously with preliminary materials.

Check box if any part of the fee is offset as provided by Exchange Act Rule 0-11(a)(2) and identify the filing for which the offsetting fee was paid previously. Identify the previous filing by registration statement number, or the Form or Schedule and the date of its filing.

(1)

Amount Previously Paid:

(2)

Form, Schedule or Registration Statement No.:

(3)

Filing Party:

(4)

Date Filed:

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5790 Widewaters Parkway  
DeWitt, New York 13214-1883

NOTICE OF ANNUAL MEETING OF SHAREHOLDERS

To the Shareholders of Community Bank System, Inc.:

Community Bank System, Inc., a Delaware corporation (the “Company”), will hold an annual meeting of shareholders at the Main Street Landing Performing Arts Center, 60 Lake Street, Burlington, Vermont 05401 on Wednesday, May 16, 2018 at 1:00 p.m. local time for the following purposes:

1.  
To elect four directors to the Board of Directors for stated terms;
2.  
To hold an advisory vote on executive compensation;
3.  
To ratify the appointment of PricewaterhouseCoopers LLP as the Company’s independent registered public accounting firm for 2018; and
4.  
To transact any other business which may properly come before the Meeting or any adjournment thereof.

The shareholders of record at the close of business on March 21, 2018, are entitled to notice of, and to vote at, the annual meeting or any adjournment or postponement thereof.

By Order of the Board of Directors

Danielle M. Cima  
Secretary  
March 29, 2018

IMPORTANT NOTICE

Please vote your shares by one of the following methods as soon as possible, whether or not you plan to attend the Annual Meeting: (1) a toll-free telephone call, (2) the Internet, or (3) the enclosed proxy in the postage paid envelope provided. If you hold shares through a broker or other custodian, please complete the voting instructions of that broker or custodian to obtain a “legal proxy.” Brokers may not vote your shares on the election of directors or the advisory vote on compensation in the absence of your specific instructions as to how to vote. Please vote your shares so your vote can be counted.

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5790 Widewaters Parkway  
DeWitt, New York 13214-1883

PROXY STATEMENT

FOR ANNUAL MEETING OF SHAREHOLDERS, MAY 16, 2018

This Proxy Statement is furnished as part of the solicitation of proxies by the Board of Directors (the “Board”) 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. local time on Wednesday, May 16, 2018, at the Main Street Landing Performing Arts Center, 60 Lake Street, Burlington, Vermont 05401. This Proxy Statement and the form of Proxy are first being sent to Shareholders on approximately March 29, 2018.

The proxy materials relating to the 2018 Annual Meeting and the 2017 Annual Report are available on the Internet. Please go to <http://ir.communitybankssystem.com/docs.aspx?iid=100185> to view and obtain the materials online.

VOTING RIGHTS AND PROXIES

The Board has fixed the close of business on March 21, 2018 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, 50,821,284 shares of common stock were outstanding and entitled to vote at the Meeting, which is the Company’s only class of voting stock. Each share of outstanding common stock is entitled to one vote with respect to each proposal to come before 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 (the “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. An abstention by a Shareholder with respect to a matter to be voted on will be counted for purposes of determining the presence of a quorum and will have the effect of a vote cast against the matter being voted on at the Meeting. Any broker non-votes will be counted as being present for purposes of determining the presence of a quorum, but will not be counted as a vote cast on the matter being voted on at the Meeting.

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.

For beneficial owners who vote their proxies by instructing their brokers or nominees, if a Shareholder instructed his or her broker or nominee to vote such shares, the beneficial owner can change his or her vote only by following the broker’s or nominee’s instructions for doing so. A beneficial owner can only change his or her vote at the Meeting if he or she has obtained a “legal proxy” from the broker or other nominee holding the shares that confirms the beneficial ownership of the shares and gives the beneficial owner the right to vote his or her shares at the Meeting.

The Company will pay its costs relating to the solicitation of Proxies. The Company has retained Alliance Advisors, LLC, 200 Broadacres Drive, 3rd Floor, Bloomfield, New Jersey 07003 to assist in soliciting Proxies for a base fee of \$6,500 plus reasonable and approved out-of-pocket expenses. Proxies may

be solicited by officers, directors, and staff members of the Company personally, by mail, by telephone, or by other electronic means. The Company will also reimburse brokers, custodians, nominees, and fiduciaries for reasonable expenses in forwarding proxy materials to beneficial owners of the Company's stock.

The Annual Report of the Company for the fiscal year ended December 31, 2017, incorporating the Form 10-K filed by the Company with the Securities and Exchange Commission ("SEC"), is being sent to Shareholders with this Proxy Statement.

#### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

Set forth below is information about the number of shares held by persons the Company knows to be the beneficial owners of more than 5% of the Company's outstanding stock as of March 21, 2018.

Name and Address of Beneficial Owner	Number of Shares of Common Stock Beneficially Owned	Percent of Class(4)
BlackRock, Inc. 55 East 52nd Street New York, NY 10055	6,532,176(1)	12.9%
The Vanguard Group, Inc. 100 Vanguard Blvd. Malvern, PA 19355	5,295,018(2)	10.4%
State Street Corporation State Street Financial Center One Lincoln Street Boston, MA 02111	3,456,544(3)	6.8%

(1)

The information is based on a Schedule 13G filed with the SEC on January 19, 2018 reporting the beneficial ownership as of December 31, 2017. BlackRock, Inc. reported that it has sole voting power with respect to 6,424,412 shares and sole dispositive power with respect to all shares listed.

(2)

The information is based on a Schedule 13G filed with the SEC on February 9, 2018 reporting the beneficial ownership as of December 31, 2017. The Vanguard Group, Inc. reported that it has sole voting power with respect to 53,327 shares and sole dispositive power with respect to 5,236,251 shares.

(3)

The information is based on a Schedule 13G filed with the SEC on February 14, 2018 reporting the beneficial ownership as of December 31, 2017. State Street Corporation reported that it has sole voting power with respect to 0 shares and sole dispositive power with respect to 0 shares.

(4)

The ownership percentages set forth in this column are based on the assumption that each of the beneficial shareholders continued to own the number of shares reflected in the table above on March 21, 2018.

**PROPOSAL ONE: ELECTION OF DIRECTORS AND INFORMATION WITH RESPECT TO DIRECTORS AND EXECUTIVE OFFICERS**

The first proposal to be acted upon at the Meeting is the election of four directors, all of whom shall hold office for three years. Directors Neil E. Fesette, Raymond C. Pecor, III, Sally A. Steele, and Mark E. Tryniski, whose terms are scheduled to expire as of the date of the Meeting, will stand for re-election. The nominees who receive the greatest number of votes “for,” represented in person or by proxy at the Meeting, will be elected directors, subject to the Company’s majority voting standard set forth below. Abstentions and broker non-votes will not have an impact on the election of directors.

Notwithstanding the application of plurality voting in the election of directors, under the Company’s majority voting standard policy adopted by the Board, if the election of directors is uncontested, a director nominee who does not receive the votes of at least the majority of votes cast with respect to such nominee’s election is expected to tender to the Board his or her resignation promptly following the certification of election results. The Governance Committee of the Board will make a recommendation to the Board whether to accept or reject such resignation. The Board will act on the resignation, taking into consideration the Governance Committee’s recommendation, and will publicly disclose the decision and its rationale within 90 days of the certification of the election results. If the Board does not accept the resignation, the director will continue to serve until his or her successor is duly elected or any earlier resignation, removal or separation. If the Board accepts the nominee’s resignation, then the Board may, in its sole discretion, fill any resulting vacancy or decrease the size of the Board pursuant to the Company’s Bylaws.

All Proxies in proper form which are received 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. In the event any nominee declines or is unable to serve, the proxy agents intend to vote for the election of a successor nominee, if any, as the Board may recommend. 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 11 members of the Board whose terms will continue beyond the Meeting (including the nominees for election at the Meeting, if elected) are expected to continue to serve on the Board until their respective terms expire or until they reach the mandatory retirement age in accordance with the Company’s Bylaws. As of December 31, 2017, the following directors retired from the Board in accordance with the Company’s mandatory retirement policy: Nicholas A. DiCerbo, James A. Gabriel, and Edward S. Mucenski.

For each nominee standing for election at the Meeting and for each director of the Company whose term of office continues after the Meeting, the Governance Committee considered the business experience set forth in the table below, as well as the additional qualifications set forth in the section entitled “Qualifications of Directors,” to determine that such director is qualified to serve on the Board.

## NOMINEES FOR DIRECTOR AND DIRECTORS CONTINUING IN OFFICE

Name and Age	Director of the Company Since	Business Experience During Past Five Years(a)	Shares of Company Common Stock Beneficially Owned(b) as of March 21, 2018(c)	Number(d)	Percent
Directors and Nominees (for term to expire at Annual Meeting in 2021)					
Neil E. Fesette Age 52	2010	President and Chief Executive Officer of Fesette Realty, LLC and Fesette Property Management in Plattsburgh, New York specializing in residential and commercial brokerage, property management, and real estate investment, development and consultation.	16,789(e)		*
Raymond C. Pecor, III Age 49	2017	President of Lake Champlain Transportation Company, a regional transportation company headquartered in Burlington, Vermont.	12,229(g)		*
Sally A. Steele Age 62	2003	Attorney, general practice with concentration in real estate, oil and gas rights, and business law, Tunkhannock, Pennsylvania; Chair of the Board of the Company.	77,980(e)		*
Mark E. Tryniski Age 57	2006	President and Chief Executive Officer of the Company. Prior service with the Company as Executive Vice President and Chief Operating Officer (March 2004 – July 2006) and Executive Vice President and Chief Financial Officer (July 2003 – February 2004). Prior to 2003, partner at the firm of PricewaterhouseCoopers LLP in Syracuse, New York.	251,948		.49%
Directors (for term to expire at Annual Meeting in 2019)					
Mark J. Bolus Age 52	2010	President and Chief Executive Officer of Bolus Motor Lines, Inc. and Bolus Freight Systems, Inc., a regional transportation company, headquartered in Scranton, Pennsylvania.	118,532(e)		*
Jeffrey L. Davis Age 65	2017	President of J.L. Davis, Inc., a construction and development firm, former President of The Champlain Valley Exposition and President of Taft Corners Associates, a development firm.	14,853(g)		*
Eric E. Stickels Age 56	2015	Former President and Chief Operating Officer of Oneida Financial Corp. (“Oneida Financial”), and President and Chief Operating Officer of Oneida Savings Bank until retirement in 2015.	61,563(f)		*
Directors (for term to expire at Annual Meeting in 2020)					
Brian R. Ace	2003	Prior to retirement in 2015, owner and operator of Laceyville Hardware, a full service	96,854(e)		*

Age 63

home product retail store in Laceyville,  
Pennsylvania.

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Name and Age	Director of the Company Since	Business Experience During Past Five Years(a)	Shares of Company Common Stock Beneficially Owned(b) as of March 21, 2018(c)	
			Number(d)	Percent
Michael R. Kallet Age 67	2015	Former Chief Executive Officer of Oneida Financial and Oneida Savings Bank until retirement in 2015.	94,226(e)(f)	*
John Parente Age 51	2010	Executive Officer of CP Media, LLC, an owner and operator of broadcast television stations, headquartered in Wilkes-Barre, Pennsylvania.	119,995	*
John F. Whipple, Jr. Age 62	2010	Chief Executive Officer of Buffamante Whipple Buttafaro, P.C., a regional certified public accounting and business advisory firm with offices in Olean, Jamestown and Orchard Park, New York.	26,317(e)	*

The following information summarizes the security ownership of named executive officers of the Bank who are not directors:

Name and Age	Business Experience During Past Five Years(a)	Shares of Company Common Stock Beneficially Owned(b) as of March 21, 2018(c)	
		Number(d)	Percent
Scott A. Kingsley Age 53	Executive Vice President and Chief Financial Officer. Prior to August 2004, Vice President and Chief Financial Officer of Carlisle Engineered Products, Inc.	93,753	*
Brian D. Donahue Age 62	Executive Vice President and Chief Banking Officer.	111,108	*
George J. Getman Age 61	Executive Vice President and General Counsel. Prior to January 2008, partner at Bond, Schoeneck & King, PLLC.	76,264	*

Joseph F. Serbun Age 57	Senior Vice President and Chief Credit Officer. Prior service with the Company as Vice President and Commercial Team Leader (January 2008 – June 2010). Prior to January 2008, Vice President at JPMorgan Chase Bank, N.A. in Syracuse, New York.	27,833	*
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 (15 persons)		1,200,246	2.34%

\*  
Represents less than .25% of the Company's outstanding shares.

(a)  
Other than (1) Mr. Tryniski who has served as a director of CONMED Corporation since 2007, (2) Mr. Kallet who served as a director of Oneida Financial from 1997 until December 2015, (3) Mr. Stickels who served as a director of Oneida Financial from December 2013 until December 2015, (4) Mr. Davis who served as a director of Merchants Bancshares, Inc. ("Merchants") from 1993 until May 2017, and (5) Mr. Pecor who served as a director of Merchants from 2012 until May 2017, no nominee or continuing Director of the Company holds, or has held in the past five years, a directorship with any public company (other than the Company) which is registered under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), or with any company which is a registered investment company under the Investment Company Act of 1940.

(b)

Represents all shares as to which the named individuals possessed sole or shared voting or investment power as of March 21, 2018. Includes shares held by, in the name of, or in trust for, the spouse and dependent children of the 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.

(c)

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. Ace holds 5,952 shares jointly with his wife, his wife holds 137 shares, and 18,790 shares are held in Mr. Ace's simplified employee pension plan; Mr. Bolus holds 48,447 shares jointly with his wife, 6,411 shares as Trustee of the Mark Bolus Trust, 4,687 shares as Trustee of the Austin Bolus Trust, 4,687 shares as Trustee of the Noah Bolus Trust, 4,686 shares as Trustee of the Paige Bolus Trust, 4,686 shares as Trustee of the Taylor Bolus Trust, and 777 shares are held by his children; Mr. Davis' spouse holds 858 shares; Mr. Donahue is the beneficial owner of 8,496 shares held by the Company's 401(k) Plan; Mr. Getman's wife holds 895 shares and he is the beneficial owner of 5,018 shares held by the Company's 401(k) Plan; Mr. Kallet is the beneficial owner of 68,404 shares held by the Company's 401(k) Plan, his wife owns 8,759 shares, and he is the trustee and one of the beneficiaries of a trust that owns 5,606 shares; Mr. Kingsley is the beneficial owner of 5,513 shares held by the Company's 401(k) Plan; Mr. Parente's children hold 30,000 shares in trusts; Mr. Pecor holds 6,392 shares in trust as trustee for trusts holding Company stock for the benefit of his niece and nephew (Mr. Pecor disclaims beneficial ownership of the shares held in these trusts); Mr. Serbun is the beneficial owner of 498 shares held by the Company's 401(k) Plan; Ms. Steele holds 48,860 shares jointly with her husband and 1,967 shares are owned jointly with her brother; Mr. Stickels' wife owns 1,730 shares and is the beneficial owner of 8,266 shares held by the Company's 401(k) Plan and he is the beneficial owner of 40,222 shares held by the Company's 401(k) Plan; and Mr. Tryniski is the beneficial owner of 17,033 shares held by the Company's 401(k) Plan.

(d)

Includes shares that the following individuals currently have the right to acquire, or will have the right to acquire within 60 days of March 21, 2018, through exercise of stock options issued by the Company: Mr. Ace, 45,972 shares; Mr. Bolus, 20,770 shares; Mr. Donahue, 63,211 shares; Mr. Fesette, 16,678 shares; Mr. Getman, 41,622 shares; Mr. Kingsley, 48,557 shares; Mr. Parente, 26,048 shares; Mr. Serbun, 16,286 shares; Ms. Steele, 23,632 shares; Mr. Tryniski, 105,048 shares; and Mr. Whipple, 26,048 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.

(e)

In addition to the number of shares of common stock reported as beneficially owned, the following Directors have elected to defer cash director fees under the director deferred compensation plan resulting in such Directors holding at risk share equivalent units ("units"), which are subject to fluctuations in the market price of the Company's stock, in the following amounts as of March 21, 2018: Mr. Ace, 17,759 units; Mr. Bolus, 3,438 units; Mr. Davis 52,585 units; Mr. Fesette, 9,369 units; Mr. Kallet, 2,368 units; Mr. Pecor, 8,006 units; Ms. Steele, 20,820 units; and Mr. Whipple, 11,090 units.

(f)

Subject to the exercise of the fiduciary duties of the Board, Messrs. Kallet and Stickels were nominated to the Board pursuant to the Agreement and Plan of Merger, dated February 24, 2015, by and between the Company and Oneida Financial.

(g)

Subject to the exercise of the fiduciary duties of the Board, Messrs. Davis and Pecor were nominated to the Board pursuant to the Agreement and Plan of Merger, dated October 22, 2016, by and between the Company and Merchants.

## CORPORATE GOVERNANCE

The Company maintains a corporate governance section on its website which contains the Company's principal governance documents including the Company's Corporate Governance Guidelines, Codes of Conduct applicable to directors, executive officers and employees, the Company's Whistleblower Policy, and the Committee Charters for the Audit and Compliance Committee, Compensation Committee, and the Governance Committee. These corporate governance documents are available on the Company's website at

<http://ir.communitybanksystem.com/govdocs.aspx?iid=100185> or a copy will be provided free of charge to any shareholder or interested party who requests a copy from the Company.

### Majority Voting Standard Policy

The Board has adopted a majority voting standard policy to provide Shareholders with a greater voice in the direction of the Company. Under the policy, if the election of directors is uncontested, a director nominee who does not receive the votes of at least the majority of votes cast with respect to such nominee's election is expected to tender to the Board his or her resignation promptly following the certification of election results. The Governance Committee will make a recommendation to the Board that it either accept or reject such resignation based on relevant considerations. The Board will act on the resignation, taking into consideration the Governance Committee's recommendation, and will publicly disclose its decision and the rationale behind its decision within 90 days of the certification of the election results. If the Board does not accept the resignation, the director may continue to serve until his or her successor is duly elected or any earlier resignation, removal or separation. If the Board accepts the nominee's resignation, then the Board may, in its sole discretion, fill any resulting vacancy or decrease the size of the Board pursuant to the Company's Bylaws.

### Director Independence

The New York Stock Exchange ("NYSE") listing standards and the Company's Corporate Guidelines require the Board to be comprised of at least a majority of independent directors. The Board has determined that 10 of the 11 Directors nominated to serve on the Board or continuing in office after the Meeting are independent under the NYSE standards and the Company's Corporate Governance Guidelines.

For a director to be considered independent, the Board must determine that the director does not have any direct or indirect material relationship with the Company. To assist it in determining director independence, the Board uses standards which conform to, or are more exacting than, the NYSE independence requirements. Under these standards, absent other material relationships, transactions or interests, a director will be deemed to be independent unless, within the preceding three years: (i) the director was employed by the Company or received more than \$120,000 per year in direct compensation from the Company, other than director and committee fees and pension or other forms of deferred compensation payments 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 fiscal year, exceeds the greater of one million dollars 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). In determining whether a director is independent, the Board reviews the stated standards but also considers whether a director has any direct or indirect material relationships, transactions or interests with the Company that might be viewed as interfering with the exercise of his or her independent judgment.

Based on these independence standards, the Board determined that the following individuals who served as directors during all or part of the last fiscal year were independent directors during such year and continue to be deemed independent by the Board: Brian R. Ace, Mark J. Bolus, Jeffrey L. Davis, Neil E. Fesette, James A. Gabriel (retired), Michael R. Kallet, Edward S. Mucenski (retired), John Parente, Raymond C. Pecor, III, Sally A. Steele, Eric E. Stickels, and John F. Whipple, Jr.

In reviewing the independence of James A. Gabriel, the Board considered the transaction described in the section entitled “Transactions with Related Persons.” The Board determined that the disclosed transaction was at market terms and pricing, consistent with the best interests of the Company and, based on the nature of the transaction, would not interfere with the exercise of Mr. Gabriel’s independent judgment.

#### Board Leadership Structure

The Company’s long-standing practice is to have a separation of the position of Chair of the Board and Chief Executive Officer. In addition, the Company maintains a Lead Director structure to provide an additional source of independent leadership for the Board in the event the Chair of the Board is not deemed to be an independent director. In the event the Chair is deemed not to be an independent director at any time, the Chair of the Audit and Compliance Committee will serve as the Lead Director of the Board and preside at executive sessions of the Board with respect to any matters which the Chair is deemed not to be independent.

The duties of the Lead Director include, but are not limited to, the following: (i) presiding at all meetings of the Board at which the Chair is not present and at executive sessions of the Board, (ii) serving as a liaison between the Chair and the independent directors, (iii) making recommendations and approving matters to be considered by the Board including agenda items, information to be provided to the Board and the schedule of meetings, (iv) authority to call meetings of the independent directors, and (v) serving as an independent point of contact for Shareholders wishing to communicate with the Board.

Both the Board Chair and Committee Chairs are subject to four year term limits, unless waived by the Board, providing for continuous development of strong leadership qualities on the Board. In addition, the Company encourages Committee Chairs and directors to participate in continuing board education opportunities and includes educational topics as a component of Board meetings over the course of each year.

#### Executive Sessions

Pursuant to the Company’s Corporate Governance Guidelines, the independent directors meet in executive sessions at the end of Board and Committee meetings as appropriate on a regular basis, without the Company’s management and non-independent directors present, to facilitate full discussion of important matters.

#### Board Committees

Among its standing committees, the Company has an Audit and Compliance Committee, a Compensation Committee, a Risk Committee, and a Governance Committee. As described more fully in the Audit Committee Report contained in this Proxy Statement, the Audit and Compliance 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, oversees regulatory compliance matters, and selects the Company’s independent auditors. The Audit and Compliance Committee held nine meetings during 2017, and its present members are Directors John F. Whipple, Jr. (Chair), Jeffrey L. Davis, and John Parente. The Board has determined that each of the Audit and Compliance Committee’s members is independent as defined by the NYSE rules.

The Company’s Compensation Committee reviews and makes recommendations to the Company’s and the Bank’s Boards regarding compensation and employee benefits matters. As described more fully in the section entitled “Compensation Discussion and Analysis,” the Compensation Committee reviews the compensation of employees in the aggregate, and the salaries and performance of named executive officers are reviewed individually. The Compensation Committee held five meetings in 2017, and its present members are Directors Neil E. Fesette (Chair), Brian R. Ace, Mark J. Bolus, and Raymond C. Pecor, III. The Board has determined that each of the Compensation Committee’s members is independent as defined by the NYSE rules. The Compensation Committee has adopted a written charter setting forth its composition and responsibilities, a copy of which is available at the Company’s website <http://ir.communitybanksystem.com/govdocs.aspx?iid=100185> and in print free of charge to any person who requests a copy.

The Company's Governance Committee evaluates and maintains corporate governance policies and makes recommendations to the Board for nominees to serve as directors. The Governance Committee will consider written recommendations by Shareholders for nominees to serve on the Board which are sent to the Secretary of the Company at the Company's main office. The Governance Committee held three meetings in 2017, and its present members are Directors Brian R. Ace (Chair), Jeffrey L. Davis, Neil E. Fesette, and John F. Whipple, Jr. The Board has determined that each of the Governance Committee's members is independent as defined by the NYSE rules. The 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 <http://ir.communitybankssystem.com/govdocs.aspx?iid=100185> and free of charge in print to any Shareholder or interested party who requests it.

In December 2016, the Board adopted changes to its corporate structure as part of the Company's preparation for the enhanced regulatory environment applicable to banks with more than \$10 billion in total consolidated assets under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank Act"). The Board created a new Risk Committee which focuses on credit risk, liquidity, and interest rate risk and an expanded role to oversee the Company's enterprise risk management functions previously addressed by the Audit/Compliance/Risk Management Committee. The Risk Committee is chaired by Director Mark Bolus and all of the directors serve on the committee. In addition, a new Stress Testing Subcommittee of the Risk Committee was formed to provide oversight of the more detailed aspects of the stress testing required by the Dodd-Frank Act, commonly known as "DFAST." Director Eric E. Stickels (Chair), Michael R. Kallet, and John F. Whipple, Jr. are members of the Stress Testing Subcommittee.

#### Qualification of Directors

In considering candidates for the Board, the Governance Committee and the Board consider the entirety of each candidate's credentials. Factors considered include, but are not necessarily limited to, outstanding achievement in a candidate's personal career; broad and relevant experience; integrity; sound and independent judgment; experience and knowledge of the business environment and markets in which the Company operates; business acumen; and willingness to devote adequate time to Board duties. The Governance Committee considers diversity in the context of the Board as a whole including gender, race, ethnicity, personal characteristics, experience and background of directors and nominees to facilitate Board deliberations that reflect a broad range of perspectives. The Board believes that each director should have an 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 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 composition of the Board as a whole.

In selecting the current directors and nominees who serve on the Company's Board, the Governance Committee considered each individual's business experience set forth below and the foregoing qualifications. In addition, the Governance Committee considered each individual's experience and knowledge of the banking and financial services industry, knowledge of and standing in key geographic markets in which the Company operates, experience and knowledge with the organization, business model and strategic plans related to the Company's success, independence in judgment and regulatory standards, special skills relevant to overall composition of the Board, including financial and accounting expertise, service with public companies, and experience in real estate and commercial finance. The Governance Committee and the Board believe that each director and nominee brings his or her own particular expertise, knowledge and experience that provides the Board as a whole with the appropriate mix of skills, characteristics and attributes to work together and fulfill the Board's oversight responsibilities to the Company's Shareholders.

The Company's Bylaws and Governance Guidelines provide for (i) a mandatory retirement age of 70, (ii) advance notice prior to serving on another public company board, and (iii) review of continued Board membership in the event of a significant change in the responsibilities or job position of a director.

The following information describes the experience and attributes held by each member of the Board relevant to his or her qualifications to serve on the Board:

Mr. Ace currently serves as the Chair of Company's Governance Committee and a member of the Compensation Committee, Risk Committee and Trust and Financial Services Committee. Mr. Ace is the former President of Laceyville Hardware and brings to the Board his business experience and an understanding of the business environment in Northeast Pennsylvania. He also has over 20 years of experience serving as a director of a national bank and previously served on the Company's Audit, Nominating and Compensation Committees. Because of this significant period of service, Mr. Ace is thoroughly familiar with the duties and responsibilities of public company audit, nominating and compensation committees and brings this knowledge and expertise to the committees on which he serves.

Mr. Bolus is the Chair of the Risk Committee and serves as a member of the Company's Compensation Committee and Strategic/Executive Committee. He is the President and Chief Executive Officer of Bolus Motor Lines, Inc. and Bolus Freight Systems, Inc., a transportation company serving the Northeastern region of the United States from its headquarters in Scranton, Pennsylvania and has 25 years of management experience in the freight transportation industry. His business experience provides the Board with insight into the economic and business environment in Upstate New York and Northeast Pennsylvania, key geographic markets for the Company. The Board also benefits from his considerable experience in real estate matters.

Mr. Davis serves as a member of the Company's Audit and Compliance Committee, Risk Committee, and Governance Committee. He has over 20 years of experience in the banking industry having served as a member of the Board of Directors of Merchants and Merchants Bank since 1993. He served as Chairman of Merchants' Board of Directors from February 2015 through May 2017. Over the course of his tenure on Merchants' Board of Directors, he has participated on its Audit, Compensation and Governance Committees. He is President of J.L. Davis, Inc., a construction and development firm, the former President of The Champlain Valley Exposition, and President of Taft Corners Associates, a development firm, and has extensive experience with the New England business environment. He is also a trustee emeritus of the University of Vermont in Burlington, Vermont, and a former president of the Vermont Special Olympics. Mr. Davis provides the Board with business and management experience, public company governance and strategic planning experience developed through his tenure on the Board of Directors of Merchants, credit knowledge, crisis and risk management experience, and an understanding of the economics of the New England region.

Mr. Fesette serves as the Chair of the Company's Compensation Committee and a member of its Strategic/Executive, Risk and Governance Committees. He is the President and Chief Executive Officer of Fesette Realty, LLC and Fesette Property Management in Plattsburgh, New York specializing in residential and commercial brokerage, property management, and real estate investment, development and consultation. He has extensive expertise in the real estate market in Upstate New York and key geographic markets where the Company operates. Plattsburgh is one of the Bank's primary regions and Mr. Fesette's knowledge regarding its economic development and areas of opportunity is a substantial benefit to the Board. Over the course of his service on the Board, Mr. Fesette has developed an expertise with corporate governance matters and succession planning, which are key skills required for his service on the Compensation and the Governance Committees. Mr. Fesette is also involved in the community and serves as a director of Champlain Valley Physicians Hospital.

Mr. Kallet is the Chair of the Trust and Financial Services Committee and serves as a member of the Risk Committee and Stress Testing Subcommittee of the Risk Committee. He has over 30 years of experience in the banking industry previously serving as the Chief Executive Officer of Oneida Financial and Oneida Savings Bank. In addition to his service as an executive, Mr. Kallet served as a director of Oneida Savings Bank and its parent company, Oneida Financial, including service as the Chair of both of the Boards. During his tenure at Oneida Savings Bank, Mr. Kallet has served as an active member of the Asset/Liability, Officer Loan, Trust Investment and Marketing Committees. Mr. Kallet is actively involved in the community and serves as Vice Chairperson of the Oneida Healthcare Center, a regional hospital headquartered in Oneida, New York. Mr. Kallet is a seasoned banker with significant knowledge and experience relating to public companies and bank holding companies and has significant ties to the Mohawk Valley region of Central New York.





Mr. Parente is the Chair of the Strategic/Executive Committee, Vice Chair of the Risk Committee and a member of the Audit and Compliance Committee. Over the course of his business career, he has developed broad expertise by serving in various management positions in a range of business ventures, including companies engaged in manufacturing, real estate, construction, banking, distribution, and media including service as the Chief Executive Officer of CP Media, LLC, an owner and operator of broadcast television stations headquartered in Wilkes-Barre, Pennsylvania. He holds an ownership interest and serves on the Board of Directors of Lackawanna Casualty Company, Lackawanna American Insurance Company, and Lackawanna National Insurance Company. He also holds an ownership interest and serves on the Board of Directors of Sordoni Construction Services and Sordoni Construction Company, regional construction companies with operations in Pennsylvania, New Jersey and New York. He developed significant banking experience through his prior involvement as a founding director of a bank located in Pennsylvania. In addition to his broad business experience, Mr. Parente provides the Board with significant risk management expertise and insights into the economic opportunities in the Northeast Pennsylvania region, which is a key geographic area for the Company.

Mr. Pecor serves as a member of the Company's Compensation Committee, Risk Committee, and Trust and Financial Services Committee. He has over eight years of experience in the banking industry having served as a member of Merchants Bank's Board of Directors from 2009 through May 2017 and a member of Merchants' Board of Directors from 2012 through May 2017. Over the course of his tenure on Merchants' Board of Directors, he has served on its Audit, Compensation and Governance Committees, and as the Chair of its Loan Committee. Mr. Pecor has significant entrepreneurial experience developed through the creation and sale of a franchise he developed in college. Currently, he is the President of Lake Champlain Transportation Company, a key regional transportation company responsible for the ferry service for the Lake Champlain area, and serves on the board of the Champlain Valley Expo. Mr. Pecor provides the Board with business and management experience, public company experience developed through his tenure on the Board of Directors of Merchants, customer service, crisis response, leadership and risk management experience, and an understanding of the Vermont market and its industries, including transportation and telecommunications.

Ms. Steele serves as the Chair of the Company's Board. She is an attorney from Tunkhannock, Pennsylvania and has extensive experience in her legal practice with natural gas drilling in the Marcellus Shale region of Pennsylvania and the economic impact of such activities in key markets for the Company. She has developed extensive public company oversight experience gained from more than 20 years of service as a director of national banks and banking holding companies. Ms. Steele has also gained significant mergers and acquisition experience through her prior board service and has a thorough understanding of the evaluation of acquisition opportunities and issues related to evaluating potential transactions. Ms. Steele provides the Board with significant corporate governance and leadership expertise through her prior experience chairing the Company's Governance Committee and her prior service on the board of another public company.

Mr. Stickels serves as the Chair of the Bank's Stress Testing Subcommittee and a member of the Risk Committee, Trust and Financial Services Committee, and Strategic/Executive Committee. He has over 30 years of experience in the banking industry previously serving in numerous positions with Oneida Savings Bank and its bank holding company, Oneida Financial, including leadership positions as President, Chief Operating Officer, Chief Financial Officer and Secretary. He also served on the Board of Directors of Oneida Financial and Oneida Savings Bank and as a member of their Asset/Liability, Trust Investment, Compliance, Information Technology, Officer Loan and Marketing Committees. Mr. Stickels has significant knowledge and experience relating to bank operations, public companies and bank holding companies and their financial reporting obligations and risk management requirements. During the course of his leadership at Oneida Financial, he gained significant risk management experience with direct supervision of the risk management programs at Oneida Savings Bank and its financial subsidiaries. Mr. Stickels' risk management experience has been a great asset to the Board and led to his selection as the Chair of the Stress Testing Subcommittee which was newly formed in 2017 as part of the Bank's preparation for crossing the \$10 billion in assets threshold. Mr. Stickels' significant financial expertise satisfies the requirements of an "audit committee financial expert" as defined in the SEC rules.

Mr. Stickels is actively involved in the community and has served as a member of the executive committee of NYSARC, Inc., a statewide non-profit provider of services for individuals with intellectual and other developmental disabilities. He also has significant ties to the Mohawk Valley region of Central New York.

Mr. Tryniski has served as the President and Chief Executive Officer (“CEO”) of the Company since 2006, and previously served the Company in the positions of Chief Operating Officer and Chief Financial Officer. Prior to joining the Company in 2003, Mr. Tryniski was a partner of PricewaterhouseCoopers LLP where he gained extensive experience in the financial service industry, manufacturing, and a broad array of business sectors. Mr. Tryniski serves as a director of a medical technology public company where he is the Chairman of the Board of Directors. He also serves on the Board of Directors of the New York Bankers Association and the New York Business Development Corporation. The Board believes that the senior officer of management should be a member of the Board. As the current President and CEO of the Company, Mr. Tryniski is familiar with all of the Company’s businesses and provides the Board with insights on all aspects of the Company’s challenges, opportunities, and operations. Because of his prior financial and business experience and with his service on another public company board, Mr. Tryniski also provides the Board with a comprehensive perspective on a broad range of business issues and additional corporate governance expertise.

Mr. Whipple is Chair of the Audit and Compliance Committee and a member of the Risk Committee, Governance Committee and Stress Testing Subcommittee. He is the Chief Executive Officer of Buffamante Whipple Buttafaro, P.C., a regional certified public accounting and business advisory firm with offices in Olean, Jamestown and Orchard Park, New York. Mr. Whipple is a certified public accountant with over 30 years of experience in advising Western New York businesses and individuals on tax planning, structuring of business transactions, financing transactions and strategic planning for businesses. The Board has deemed him an “audit committee financial expert” as defined by the SEC rules. Mr. Whipple provides the Board with significant management experience, as well as expertise with respect to corporate finance, accounting and the analysis of public company financial statements and related SEC filings.

#### Communication with Directors

Shareholders and any interested parties may communicate directly with the Board by sending correspondence to the address shown below. In addition, Shareholders or interested parties may contact or communicate with the Company’s Lead Director, John F. Whipple, Jr., as a representative of the independent directors in the same manner. The receipt of any such correspondence addressed to the Board 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 or an interested party 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 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

#### Stock Ownership Guidelines

In 2017, the Board approved and enhanced the stock ownership guidelines for senior executives of the Company. The revised stock ownership guidelines require (i) the CEO to own shares of Company common stock and share equivalents equal to at least four times his base salary, and (ii) the Chief Financial Officer and other Executive Vice Presidents to own shares of common stock or share equivalents equal to at least two times their base salary. Senior executive officers are required to retain shares received from stock option exercises or other equity awards, net of taxes, until they have satisfied the equity ownership requirements. All executive officers exceed the requirements of the stock ownership guidelines established by the Company.

The Board has also adopted revised stock ownership guidelines for directors of the Company. The guidelines require each director to own shares of Company common stock and share equivalent units equal in value to at least five times the annual base Board member retainer within six years of becoming a director. Under the guidelines, the qualifying share equivalent units consist of at risk units resulting from the director's deferment of cash director fees under the deferred compensation plan. In addition, new directors are required to own at least \$25,000 of common stock within one year of joining the Board. All directors exceed the requirements of the stock ownership guidelines.

#### Board's Role in Risk Management Oversight

The Company does not view risk in isolation, but considers risk as part of its regular consideration of business strategy and business decisions. Assessing and managing risk is the responsibility of the Company's management, which establishes and maintains risk management processes, controls, and policies to balance risk mitigation and creation of shareholder value. The Board oversees and reviews various aspects of the Company's risk management efforts, either directly or through its committees, and exercises its risk oversight function in several ways. The Board reviews and approves various policies that address and mitigate material risks. This includes policies addressing credit risk, interest rate risk, investment risks, liquidity risks, operational risks, strategic risks and compliance/legal risks, among other matters. The Board also reviews and monitors enterprise risks through various reports presented by management, internal and external auditors, and regulatory examiners.

While the Board has primary responsibility for the oversight of the Company's risk management, the Board's standing committees support the Board by regularly addressing various risks in their respective areas of oversight. Specifically, the Company's Risk Committee assists the Board in fulfilling its oversight responsibilities with respect to risk management in its oversight of various functions including review of periodic reports from management on risks related to credit risk, interest rate risk, liquidity risk, information technology, enterprise risk management, the Company's corporate insurance program, lending activities, asset quality and the investment portfolio. The Audit and Compliance Committee approves and reviews the engagements and periodic reports of the Company's independent auditor and internal audit department related to the Company's financial statements and oversees areas of regulatory compliance, including Sarbanes-Oxley compliance. The Compensation Committee reviews and considers risks related to the Company's compensation policies, including incentive plans to determine whether these plans subject the Company to excessive risks. The Governance Committee considers only director candidates with appropriate experience and temperament and continues to ensure appropriate corporate governance policies are in place. Each of the committee chairs updates the full Board at regular meetings concerning the activities of the committee, the significant issues it has discussed and the actions taken by the committee.

#### Compensation of Directors

The Board has adopted an all retainer-based compensation structure based on the recommendation of the Compensation Committee with input from Pearl Meyer & Partners ("Pearl Meyer"), an independent compensation consultant engaged by the Compensation Committee. The following table sets forth the annual retainer fees paid to the directors for their service on the Board and the various committees on which they serve in 2017:

Position	Board	Audit and Compliance Committee	Compensation Committee	Risk Committee	Governance Committee	Strategic/ Executive Committee	Stress Testing Sub-Committee	Trust and Financial Services Committee
Chair	\$ 90,000	\$ 17,500	\$ 12,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000	\$ 10,000
Member	\$ 50,000	\$ 8,500	\$ 6,000	None	\$ 5,000	None	\$ 5,000	\$ 5,000

In 2018, based on a review and assessment of director compensation in late 2017 by Pearl Meyer, as an independent consultant to the Compensation Committee, the Board adopted the following changes to certain annual retainers: the Chair's annual retainer was increased by \$10,000 to \$100,000; the Chair of the Audit and Compliance Committee's annual retainer was increased by \$2,500 to \$20,000 and its committee members' annual retainer was increased by \$1,500 to \$10,000; and the Chair of the Compensation Committee's annual retainer was increased by \$2,000 to \$14,000 and its committee members' annual retainer was increased by \$1,000 to \$7,000.

The Company pays the travel expenses incurred by each director in attending meetings of the Board. Any executive officer serving on the Board does not receive compensation for attending Board and committee meetings.

Consistent with aligning director compensation with the long-term interests of Shareholders, the directors also receive a portion of their total compensation in the form of equity grants under the Company's 2014 Long-Term Incentive Compensation Program, as amended (the "2014 Incentive Plan"). Starting in 2016, the directors could elect to receive the equity component of their compensation in the form of deferred stock units or non-statutory stock options of an equivalent amount. The Board believes that providing part of the directors' compensation in the form of an annual equity award is consistent with the Company's overall compensation philosophy of aligning the interests of individual directors with the long-term interests of the Company's Shareholders, and enables the Company to continue to attract highly qualified individuals to serve on the Board.

The equity award grants reflected in the Director Compensation Table below were made under the 2014 Incentive Plan which allows for the issuance of deferred stock units and stock option grants in an amount determined by the Compensation Committee. Directors can elect to take their equity grants in the form of deferred stock units or stock options. The fair value of the deferred stock units and stock options are equivalent as of the grant date with the value of the annual equity award being determined by the Compensation Committee. Each stock option granted to a director is granted at an option price per share equal to the fair market value on the date of grant, and is exercisable on the 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 remains exercisable after the grant date 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. Directors electing to take their equity award in the form of deferred stock units (in lieu of stock options) are allowed to defer receipt of the units to a future date of up to ten years following the grant date. The value of the deferred stock units track the market value of the Company stock and are ultimately paid out in shares of the Company stock on the deferred payment date. The director equity grants, in either the form of stock options or deferred stock units, are designed to provide a reasonable component of total director compensation that aligns director compensation with the long-term interests of the Shareholders.

The following table summarizes the annual compensation paid to each non-employee director for his or her service to the Board and its committees in 2017. The Company does not make payments (or have any outstanding commitments to make payments) to director legacy programs or similar charitable award programs.

#### DIRECTOR COMPENSATION

Name(1)	Fees Earned or Paid in Cash (\$)	Deferred Stock Awards \$(2)	Stock Option Awards \$(3)	Total (\$)
Brian R. Ace	\$ 65,000	\$ 31,587	\$ 0	\$ 96,587
Mark J. Bolus	\$ 61,000	\$ 31,587	\$ 0	\$ 92,587
Jeffrey L. Davis	\$ 41,750	\$ 0	\$ 0	\$ 41,750
Nicholas A. DiCerbo	\$ 65,000	\$ 31,587	\$ 0	\$ 96,587
Neil E. Fesette	\$ 67,000	\$ 31,587	\$ 0	\$ 98,587
James A. Gabriel	\$ 62,500	\$ 0	\$ 31,669	\$ 94,169
Michael R. Kallet	\$ 60,000	\$ 31,587	\$ 0	\$ 91,587
Edward S. Mucenski	\$ 78,500	\$ 31,587	\$ 0	\$ 110,087
John Parente	\$ 68,500	\$ 0	\$ 31,669	\$ 100,169
Raymond C. Pecor, III	\$ 40,500	\$ 0	\$ 0	\$ 40,500
Sally A. Steele	\$ 90,000	\$ 31,587	\$ 0	\$ 121,587
Eric E. Stickels	\$ 65,000	\$ 31,587	\$ 0	\$ 96,587

John F. Whipple, Jr.	\$ 68,500	\$ 0	\$ 31,669	\$ 100,169
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(1)

Mark E. Tryniski, President and CEO, does not receive any compensation for his service as a director. Mr. Tryniski's compensation is set forth in the Summary Compensation Table.

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(2)

The amounts in this column reflect the grant date fair value of deferred stock units computed in accordance with FASB ASC Topic 718 for equity awards granted in 2017 pursuant to the 2014 Incentive Plan. The deferred stock unit award was made and vested on March 15, 2017. As of December 31, 2017, each director had the following number of deferred stock units outstanding: Mr. Ace 2,384; Mr. Bolus 1,473; Mr. DiCerbo 1,474; Mr. Fesette 2,384; Mr. Kallet 1,473; Mr. Mucenski 2,384; Ms. Steele 563; and Mr. Stickels 563.

(3)

The amounts in this column reflect the grant date fair value of non-statutory stock options computed in accordance with FASB ASC Topic 718 for equity awards granted in 2017 pursuant to the 2014 Incentive Plan. The option award was made and vested on March 15, 2017, and the exercise price is \$57.12. As of December 31, 2017, each director had the following number of options outstanding: Mr. Ace 45,972; Mr. Bolus 20,770; Mr. Davis 0; Mr. DiCerbo 7,877; Mr. Fesette 16,678; Mr. Gabriel 42,089; Mr. Mucenski 10,678; Mr. Parente 23,489; Mr. Pecor 0; Ms. Steele 23,632; Mr. Stickels 0; and Mr. Whipple 23,489.

Directors may elect to defer all or a portion of their cash director fees pursuant to the Company's 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 the Company's 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 Company stock, 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 the Shareholders. No earnings are deemed above-market or preferential on compensation deferred under the Deferred Compensation Plan for the Directors. Directors currently participating in the plan hold at risk share equivalent units (based on cash fees directors have deferred under the plan), which are subject to market price fluctuations in the Company's stock in the following amounts as of December 31, 2017: Mr. Ace 20,712 units; Mr. Bolus 2,406 units; Mr. DiCerbo 54,824 units; Mr. Fesette 9,311 units; Mr. Kallet 2,354 units; Mr. Mucenski 9,734 units; Ms. Steele 23,627 units; and Mr. Whipple 11,022 units.

#### Transactions With Related Persons

Various directors, executive officers and other related persons of the Company and the Bank (and members of their immediate families and corporations, trusts, and other entities with which these individuals are associated) are indebted to the Bank through business and consumer loans offered in the ordinary course of business by the Bank. All such loans were made in the ordinary course of business, were made on substantially the same terms, including interest rates and collateral, as those prevailing at the time for comparable loans with persons not related to the Bank, and did not involve more than the normal risk of collectability or present other unfavorable features. The Company expects that the Bank will continue to have banking transactions in the ordinary course of business with its directors, executive officers and other related persons on substantially the same terms, including interest rates and collateral, as those then prevailing for comparable transactions with others.

During the year ended December 31, 2017, the law firm of Franklin & Gabriel, owned by retired Director James A. Gabriel, provided legal services to the Bank's operations in its Finger Lakes markets and the law firm of DiCerbo Morgan, PLLC, of which retired Director Nicholas A. DiCerbo is an attorney, provided legal services to the Bank's operations in its Southern Region markets. For services rendered during 2017 and for related out-of-pocket disbursements, the law firm of DiCerbo Morgan, PLLC received approximately \$550,000 and the law firm of Franklin

& Gabriel received less than \$100,000 from the Bank

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for transactional and specialized commercial legal services and related loan closings with customers of the Bank. All of these relationships and transactions relate to the provision of legal services in connection with, and in support of, the Bank's lending business in local and regional markets where the law firms are established and well-recognized in the communities. Both Mr. DiCerbo and Mr. Gabriel retired from the Board effective December 31, 2017 and these relationships are no longer subject to the Company's related person transaction policy described below.

The Company has a Related Party Transaction Policy, administered by the Audit and Compliance Committee, which provides procedures for the review and approval of related party transactions involving the Company's directors, executive officers, director nominees, and other related persons. In deciding whether to approve such related party transactions, the Audit and Compliance Committee will consider, among other factors it deems appropriate, whether the transaction is on terms comparable to those generally available to nonaffiliated parties and is consistent with the best interests of the Company. For purposes of this policy, a "related party transaction" is a transaction, arrangement, or relationship or series of similar transactions, arrangements or relationships in which (i) the Company or one of its subsidiaries is involved, (ii) the amount involved exceeds \$100,000 in any calendar year, and (iii) a related party has a direct or indirect material interest. Related persons include executive officers, directors, director nominees, beneficial owners of more than 5% of the Company's stock, immediate family members of any of the foregoing persons, and any firm, corporation or other entity in which any of the foregoing persons has a direct or indirect material interest. All of the related person transactions with the named directors were reviewed and approved by the Audit and Compliance Committee after the Committee determined that the transactions were performed at market terms and were consistent with the best interests of the Company.

#### Compensation Committee Interlocks and Insider Participation

Mark J. Bolus, Neil E. Fesette, Edward S. Mucenski (retired), and Raymond C. Pecor, III served on the Compensation Committee for all or part of 2017. There were no Compensation Committee interlocks or insider (employee) participation during 2017.

#### Director Meeting Attendance

The Board held seven regular meetings and no special meetings during the fiscal year ended December 31, 2017. 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 directors attended the Company's Annual Meeting of Shareholders held on May 17, 2017.

#### Code of Ethics

The Company has a Code of Ethics for its directors, officers and employees. The Code of Ethics requires that individuals avoid conflicts of interest, comply with all laws and other legal requirements, conduct business in an honest and ethical manner, and otherwise act with integrity and in the best interests of the Company. In addition, the Code of Ethics requires individuals to report illegal or unethical behavior they observe.

The Company also has adopted a Code of Ethics for Senior Executive Officers that applies to its chief executive officer, chief financial officer, and other senior officers performing similar functions. This Code of Ethics is intended to promote honest and ethical conduct, full and accurate reporting, and compliance with laws and regulations.

The text of each Code is posted on the Company's website at <http://ir.communitybankssystem.com/govdocs.aspx?iid=100185> and is available in print free of charge to any Shareholder or interested party who requests it. The Company intends to report and post on its website any amendment to or waiver from any provision in the Code of Ethics for Senior Executive Officers as required by SEC rules.

## COMPENSATION DISCUSSION AND ANALYSIS

## Introduction

This section contains a description and analysis of the Company's executive compensation policies and practices. The Compensation Committee of the Board reviews and administers the Company's compensation policies and practices for the executive officers of the Company, including the individuals listed in the compensation disclosure tables (the "named executives"). The Compensation Committee currently consists of four members of the Board, each of whom is an independent, non-employee director.

In administering compensation policies and practices, the Committee seeks to (i) link pay and performance with Company executives having the opportunity to earn total compensation commensurate with the Company's performance, (ii) align executives' interests with those of the Company's Shareholders, (iii) retain key executive talent, and (iv) ensure compensation policies, and incentive plans, do not motivate excessive risk taking. The Committee seeks to achieve its objectives by using a combination of incentive-based cash and equity award components focused on short-term tactical goals and longer term performance goals tied to creation of shareholder value.

The Company provides its Shareholders with the opportunity to cast an annual advisory vote on executive compensation (a "say-on-pay proposal"). At the Company's Annual Meeting of Shareholders held in May 2017, approximately 97% of the votes cast on the say-on-pay proposal at that meeting were voted in favor of the Company's executive compensation program. The Compensation Committee believes this vote affirms the Shareholders' support of the Company's approach to executive compensation; however, the Committee will continue to oversee the executive compensation programs consistent with the objectives set forth herein and consider the outcome of the Company's future say-on-pay votes, regulatory changes and emerging best practices when making future compensation decisions for the named executives.

## Executive Summary

The Company delivered strong operating performance in fiscal year 2017 and continued positive trends and performance in many areas including operating earnings, credit quality, revenue growth, expense management and dividends declared:

	2017	2016	Percentage Change
Net Interest Income	\$315.7 million	\$273.9 million	15.3%
Non-interest Income	\$202.4 million	\$155.6 million	30.1%
Total Operating Expenses(1)	\$321.2 million	\$265.1 million	21.2%
Net Income	\$150.7 million	\$103.8 million	45.2%
Diluted Earnings per Share	\$3.03	\$2.32	30.6%
Net Charge-Offs/Average Loans	0.18%	0.13%	38.5%
Dividends Declared per Share	\$1.32	\$1.26	4.8%

(1)

Excluding acquisition expenses.

The Company has consistently returned significant value to its Shareholders. Its total annualized shareholder returns as compared to bank-specific and general indices over multiple periods over the past 15 years are set forth below:

Total Shareholder Returns(1)(2)

	2 Year	5 Years	10 Years	15 Years
Community Bank System	19.0%	17.9%	14.5%	12.4%
S&P 600 Commercial Bank Index	18.9%	18.7%	6.0%	5.1%
KBW Regional Bank Index	19.0%	17.7%	6.3%	6.0%
S&P 500 Index	16.8%	15.8%	8.5%	9.9%
Dow Jones Industrial Average Index	22.1%	16.4%	9.3%	10.2%

(1)

Annual equivalent through December 31, 2017, including reinvestment of dividends.

(2)

Source: Bloomberg, L.P.

In August 2017, the Company increased its quarterly cash dividend to Shareholders by 6.3%, to \$0.34 per share, marking its 25th consecutive year of annual increases.

After considering the Company's operating performance and return to Shareholders, the Compensation Committee took the following actions relating to 2017 performance and structuring incentive compensation with regards to its named executives and key employees:

- Approved annual cash incentive awards at the level of 135% of the target amount in line with performance measured against pre-established performance objectives, as described on pages 24 to 26; and

- Granted stock options and restricted stock awards at the target amount based on the determination that the Company's performance was above the pre-established performance goals, as described on pages 26 to 27. These equity awards are subject to a five year pro rata vesting schedule and, with respect to the stock options, require stock price appreciation in order to have value.

- Reviewed and approved levels of executive compensation and the terms for renewal of a three year employment agreement with the Company's President and CEO, Mark E. Tryniski, with input from the executive compensation firm of Pearl Meyer, serving as an independent compensation consultant, as described on page 23.

#### Role of Compensation Committee, Compensation Consultants and Executive Officers

The Compensation Committee is responsible for the development, oversight and administration of the Company's compensation and benefit programs. In carrying out its duties, the Committee reviews and approves the Company's goals and objectives with respect to the CEO and other executives and seeks to align compensation with the Company's business objectives and performance. The Compensation Committee also evaluates the performance of the CEO and the other executives in light of such goals and objectives and determines compensation levels based on such evaluation. The Committee also oversees the administration of broad-based compensation plans for the Company and its subsidiary entities, the review of succession planning for key positions in the Company, and the review and approval of executive level employment agreements subject to approval by the Board.

The Compensation Committee has the resources and authority appropriate to discharge its duties and responsibilities, including the ability pursuant to its charter to select and retain the services of independent compensation consultants in its sole authority. The Committee retained Pearl Meyer in January 2017 to serve as an independent advisor with

respect to executive and Board compensation. In particular, Pearl Meyer has been engaged to: (i) assess the Company's executive compensation and performance compared to the market and the Company's peers, (ii) review executive pay and performance alignment for the CEO, the Chief Financial Officer ("CFO"), the General Counsel, and the Chief Banking Officer, and (iii) make

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recommendations related to total compensation for this group of executive officers. Pearl Meyer presented the results of its reviews and recommendations to the Compensation Committee at its meetings in October and November 2017 for the Committee's use in determining the appropriateness of the Company's executive compensation compared to market and performance, in particular the appropriateness of Mr. Tryniski's compensation in connection with the review and renewal of his employment agreement.

The Committee has also retained Pearl Meyer to review and provide advice on the structure and level of compensation for directors in connection with the Committee's review of director compensation for 2018. The purpose of the engagement was to assess whether the current Board compensation program is competitive and appropriate and to better understand emerging practices and considerations for potential areas of modification.

The Committee has assessed the independence of Pearl Meyer pursuant to SEC rules and concluded that no conflict of interest exists that would prevent Pearl Meyer from service as an independent advisor to the Committee. Pearl Meyer provided no services to the Company or its management other than services related to the Company's compensation programs.

Although the Compensation Committee makes independent determinations on all matters related to compensation of the named executives utilizing executive sessions without management present, certain members of management are requested to attend and provide input to the Committee throughout the year. The Compensation Committee receives input from Company management, including the CEO, CFO, Chief Human Resources Officer, General Counsel and others as needed to ensure that it has the information and perspective needed to carry out its duties.

At the beginning of each fiscal year, the Compensation Committee discusses the Company's performance and sets performance goals and objectives with the input and recommendation of the CEO for the Company's short-term Management Incentive Plan ("MIP"). In monitoring performance during the course of the year, the Committee receives updates and information from the CFO to verify and track the Company's financial performance and progress in achieving the objectives established under the MIP plan. The Committee uses such information in monitoring performance and ultimately determining the annual incentive compensation awards earned by named executives and participants under the MIP plan at the end of the fiscal year.

#### Philosophy and Objectives

The Company's ability to attract and retain talented employees and executives with the skills and experience to develop and execute business opportunities is essential to its success and providing value to its Shareholders. The Company seeks to provide fair and competitive compensation to its employees by structuring compensation principally around two general parameters. First, compensation is targeted to be near the median of the market. Second, when the Company exceeds its performance goals and peers, the Company's total compensation is designed to reward employees with pay above median. Similarly, if the Company's performance does not meet its goals or falls below its peers, the Company's compensation is designed to fall below median. To support this pay-performance alignment, a significant amount of the Company's executives' total compensation is incentive based and tied to the achievement of Company performance goals and long-term Shareholder value. The Company believes pay-performance alignment should be evaluated over a multiple year period since much of its pay is related to longer-term performance results.

The Compensation Committee structures the annual cash incentive and equity-based elements of the compensation program to promote the achievement of the Company's long-term growth goals, including improvement in earnings per share ("EPS") each year, improvement in return on equity, and achievement of total shareholder returns at or above its peer group's returns. EPS is generally defined as the Company's net income divided by the weighted average number of shares outstanding during that period. The Company believes EPS reflects the best measurement of its performance and progress towards continuously increasing Shareholder value.

The Company's executive compensation program seeks to:

1.  
Attract, retain and motivate highly qualified executives through both short-term and long-term incentives that emphasize overall Company and group performance;
2.  
Provide incentives to increase Shareholder value by:
  - aligning incentive compensation to financial and non-financial performance measures tied to creation of Shareholder value; and
  - utilizing equity-based compensation to encourage its executives to have an ownership perspective and align their interests with those of the Company's Shareholders;
3.  
Manage compensation costs through the use of performance-based compensation tied to corporate and individual performance criteria focused on sustainable long-term earnings growth of the Company;
4.  
Structure compensation criteria so that achievement of corporate and individual goals do not encourage excessive risk taking;
5.  
Prohibit any tax gross-up provisions in employment-related agreements and limit perquisites and personal benefits to those that support the business function of the executive; and
6.  
Require senior executives to retain substantial amounts of the Company's stock in proportion to such executive's position with the Company pursuant to its stock ownership policy.

#### Policies and Procedures

To achieve the compensation program's objectives, the Company utilizes the following policies and procedures. The Company seeks to provide competitive compensation based on market data. The Company compares its cash, equity and benefits-based compensation practices with those of other companies of similar size operating in similar geographic market areas. The Compensation Committee considers various industry surveys including the American Bankers Association, the New York Bankers Association Compensation Report, and McLagan Financial Services Industry Survey, and compensation benchmarking resources through Economic Research Indicators (ERI), to confirm the appropriateness of overall compensation levels and the components of compensation for executives. The Compensation Committee utilizes multiple sources of data, as well as engaging independent compensation consultants from time to time for independent analysis and input regarding benchmarking the Company's compensation programs with comparable financial institutions. The Compensation Committee retained the services of Pearl Meyer to serve as an independent compensation consultant in 2017 as described on pages 19 to 20. The Company encourages teamwork. The Company recognizes that its long-term success results from the coordinated efforts of employees, working towards common, well-established objectives. While individual accomplishments are encouraged and rewarded, the performance of the Company as a whole is a determining factor in total compensation opportunities. The Company strives for fairness in the administration of compensation. The Company strives to ensure that compensation levels accurately reflect the level of responsibility that each individual has within the Company.

Executives are informed of individual and Company-wide objectives.

Goal setting, performance review and aligning variable pay to performance. Performance assessment involves the following:

1.

At the beginning of each fiscal year, the Company's CEO distributes written performance goals and objectives as approved by the Compensation Committee and the full Board. Performance goals include specific financial and operational objectives for the Company.

2.

All performance goals are reviewed on an ongoing basis to ensure that the Company is responding to changes in the marketplace and economic climate, and that progress is assessed on a continuing basis over the course of the year.

3.

At the end of the fiscal year, Company and individual performance is evaluated against the established goals. These evaluations, as well as consideration of the responsibilities associated with an individual's position, affect decisions on the individual's base salary, cash incentive, and equity-based compensation.

#### Compensation Best Practices

The Company continues to implement its executive compensation program in a manner that is designed to reinforce its philosophy of aligning each named executive's compensation with the Company's short-term and long-term performance. The Company uses the following practices in order to align its compensation philosophy with those practices generally considered to promote Shareholder value:

- Pay for performance. A significant percentage, 62% for the CEO, of the named executive's total compensation varies with Company performance.

- Correlation between incentive compensation, performance measures, and strategic objectives. Performance measures for the MIP and long-term equity-based incentive compensation are tied to a balance of both strategic and near-term operating objectives designed to create long-term Shareholder value.

- Manage Risk. The Compensation Committee reviews all incentive compensation plans on an annual basis to ensure such plans do not encourage excessive risk taking.

- Significant stock ownership requirements. The CEO and senior executives are subject to the Company's stock ownership requirements set forth on pages 13 to 14.

- Limited perquisites. The Company provides limited perquisites to its named executives only on the basis of a sound business rationale.

- Policy on insider trading that prohibits hedging of Company securities. The Company prohibits its named executives and directors from pledging shares on margin, trading in derivative securities of the Company's common stock, or hedging with respect to Company stock.

- "Double trigger" in the event of a change in control. The Company's change in control provisions are "double-triggered," requiring a change in control and a subsequent involuntary termination without cause or voluntary termination for good reason in order for the named executive to become entitled to compensation and benefits under the change in control provision.

- Clawback of certain compensation in the event of restatement. The senior executives and other employees are subject to the Company's recoupment policy ("clawback") for incentive compensation in the event of certain financial restatements.

- No tax gross ups. The Company does not provide tax "gross-ups" to its executives in any plan or agreement.



#### Benchmarking Against the Company's Peer Group

Understanding the industry's landscape is an essential element of establishing the Company's program targets and making compensation decisions. The Company regularly review competitive market data and compare executive pay and performance to market norms to ensure alignment. The Compensation Committee engaged Pearl Meyer in 2017 to determine a group of the Company's peers in order to assess the Company's programs and pay levels for senior executives against 21 publicly traded banks similar in regional location and asset size to the Company (the "Peer Group"). The Peer Group consists of the following companies: Berkshire Hills Bancorp Inc., Chemical Financial Corporation, First Commonwealth Financial Corporation, First Financial Bancorp., First Merchants Corporation, First Midwest Bancorp, Inc., F.N.B. Corporation, Fulton Financial Corporation, Independent Bank Corp., MB Financial, Inc., NBT Bancorp, Inc., Old National Bancorp, Park National Corporation, S&T Bancorp, Inc., Sterling Bancorp, Union Bankshares Corporation, United Bankshares, Inc., Valley National Bancorp, Webster Financial Corp., WesBanco, Inc., and Wintrust Financial Corporation. The Compensation Committee used

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this Peer Group information in making determinations regarding the 2018 base salaries for the named executives and in particular the compensation set forth in Mr. Tryniski's new employment agreement, which is discussed in the "Renewal of President and CEO's Employment Agreement" section below.

#### Renewal of President and CEO's Employment Agreement

The Compensation Committee reviewed and approved the terms of a new three year employment agreement with the Company's President and CEO, Mr. Tryniski, which agreement became effective on January 1, 2018 and continues to December 31, 2020. This agreement replaces the employment agreement which expired on December 31, 2017. The terms of Mr. Tryniski's new employment agreement are described on page 39.

In connection with reviewing Mr. Tryniski's employment agreement, the Committee engaged the independent executive compensation firm of Pearl Meyer to conduct a competitive review of compensation for senior executives which included an assessment of Mr. Tryniski's compensation compared to peers and a review of CEO pay and performance alignment. Pearl Meyer's review found that the Company's performance continues to perform above the Peer Group median performance levels for total shareholder returns, return on assets, return on equity, net interest margin, and efficiency ratio (the Peer Group is set forth above). In addition, in reviewing the relationship between CEO compensation and the Company performance, it was noted that the Company's performance based on three-year total shareholder return ranked ninth in the Peer Group, while Mr. Tryniski's total compensation ranked 15th in the Peer Group. Pearl Meyer noted that the short-term and long-term incentive opportunities slightly lagged the market. Following review of all considerations and the long term performance of the Company, the Committee approved an increase in Mr. Tryniski's total compensation to slightly less than the 55th percentile in the Peer Group, effective as of January 1, 2018.

#### Overview of the Company's Compensation Program

The Company's business model is to offer financial products and services of a comprehensive and sophisticated nature while providing a level of customer service which exceeds the service quality delivered by other financial institutions in its markets. The delivery of those products and services, in ways that enhance Shareholder value, requires that the Company attract key people, promote teamwork, and reward results. To further these goals, the Company maintains the following compensation programs.

#### Cash-Based Compensation

**Salary.** The Company sets base salaries for employees by reviewing the total cash compensation opportunities for comparable positions in the market. Its objective is to pay salaries that are commensurate with market levels and recognize the role, experience, performance and contributions of each executive to the Company's success.

**Management Incentive Plan.** In order to focus and reward its key management for achievement of the Company's annual business objectives, the Company provides a portion of compensation that is tied to its performance. The management incentive plan covers the Company's key management and officers and during 2017 approximately 35% of the Company's employees participated in the MIP. Incentive award levels, expressed as a percentage of salary, are established for different organizational levels within the Company. For the named executives, their respective awards reflect a combination of the Company's performance relative to corporate wide financial and tactical objectives and their own performance as discussed on pages 24 to 26.

**Equity-Based Compensation.** The Company uses equity-based compensation, including stock options and restricted stock, as a component of total compensation, to align the interests of management with those of the Shareholders. The Board typically awards equity-based compensation on an annual basis, although grants are not guaranteed and are made at the discretion of the Compensation Committee. Equity awards are targeted to reflect a percentage of salary which has been established for different organizational levels within the Company based on market practice and its desire to focus a meaningful portion of total compensation in long-term, stock-based compensation. Equity awards typically consist of a combination of time and performance vested restricted stock and stock options. This portfolio approach helps achieve multiple objectives focused on (i) aligning value of grants with future performance (stock price and

predefined performance goals), (ii) encouraging stock ownership, and (iii) providing retention incentives for the Company's top talent. Stock options and restricted stock can also serve as an effective tool in recruiting key individuals to work for the Company and vesting requirements encourage those individuals to continue in the employ of the Company. The Company has, on occasion, issued limited amounts of restricted stock to individuals to support specific business objectives, including rewarding performance in special assignments and recognizing extraordinary service in consummating acquisitions. The Company utilizes both time and performance criteria in the vesting conditions for stock options and restricted shares to better correlate equity compensation with the long-term performance of the Company.

#### Benefits

All salaried employees participate in a variety of retirement, health and welfare, and paid time-off benefits designed to enable the Company to attract and retain a talented workforce in a competitive marketplace. These benefits and related plans help ensure that the Company has a productive and focused workforce. The Company utilizes a retirement and 401(k) savings plan to enable employees to plan and save for retirement.

The Company's tax-qualified 401(k) employee stock ownership plan (the "401(k) Plan") allows employees to contribute up to 90 percent of their base salaries to the 401(k) Plan on a pre-tax or after-tax basis, subject to various limits imposed by the Internal Revenue Code. The Company provided a matching contribution up to 4.5 percent of the contributing participant's salary in 2017 subject to various limits imposed by the Internal Revenue Service ("IRS").

#### Compensation of the Named Executives

The compensation program for senior executives is built around the philosophy of targeting market-median compensation with variable incentive components that vary above or below market to reflect Company and individual performance. The Company's compensation program consists of three primary elements:

- base salary;
- annual cash bonus pursuant to the MIP; and
- equity-based long-term incentives.

Consistent with the Company's goal to emphasize performance-based and variable compensation, as a group, approximately 48% of Messrs. Tryniski's, Kingsley's, Donahue's, Getman's and Serbun's 2017 compensation is attributable to base salary and approximately 52% is attributable to variable performance-based incentive compensation (consisting of annual bonus and equity awards).

#### Base Salary

The Company uses the base salary element of total compensation to provide the foundation of a fair and competitive compensation opportunity for each individual named executive. Each year, the Company reviews base salaries and targets salary compensation at or near the median base salary practices of the market, but maintains flexibility to vary from market-median practices to reflect individual performance and contributions. Generally, the Compensation Committee starts the total compensation review for executives by reviewing any identified compensation trends and any recommendations with respect to the base salary of named executives. The Committee recognizes that base salaries are the foundation for many other pay programs to the extent they are expressed as percentages of base salary (e.g., the cash incentive under the MIP is a percentage of the executive's base salary). As a result, the Committee carefully considers the appropriate base salaries amounts to ensure proper pay mix and positioning.

#### Annual Incentive Payments under the Management Incentive Plan (MIP)

Annual incentives under the MIP are designed to be awarded upon the satisfaction of performance-based achievements relative to specified Company performance goals. The Compensation Committee retains discretion to adjust awards based on factors related to the Committee's assessment of the Company's performance, management's overall performance as a group, individual performance, and



risk assessment of performance goals. The Compensation Committee may also take into account management's performance in addressing unanticipated matters, general economic conditions and industry-specific factors, and other factors deemed relevant by the Committee.

The predominate metric in the Compensation Committee's evaluation of performance is a review of the achievement of the predetermined annual corporate goals. The goals are intended to focus management's strategic priorities in the operation of the Company. Accordingly, the compensation of each executive officer is based predominantly on the assessment of the achievement of these predetermined corporate goals.

At the beginning of each fiscal year, the Compensation Committee establishes the annual corporate performance goals. Corporate goals are proposed by the CEO, reviewed and approved by the Committee and also approved by the Board on an annual basis. The Committee considers and assigns a relative weight to appropriately focus efforts on corporate goals that are intended to enhance Shareholder value. Over the course of the year, the Committee receives periodic updates on the progress towards achieving the predetermined corporate goals. Prior to approving payment of the incentive bonuses for 2017, the Committee evaluated the Company's performance by assessing if, and the extent to which, the Company achieved or failed to achieve the corporate goals approved by the Board at the beginning of fiscal year 2017. Based on its assessment of performance in achieving the predetermined goals and other factors deemed to be relevant, the Committee determined that the Company's performance was above target level by 35% resulting in awards for the 2017 year (paid in 2018) equivalent to 135% of the target amount.

The Company's corporate goals for payments made under the 2017 MIP and the level at which the Compensation Committee determined they were achieved are as follows:

Corporate Goal	Minimum Threshold and Maximum Achievement Levels	Achievement Level	2017 Achievement
Improvement in operating earnings per share above prior year	Minimum: Greater than 1% improvement Maximum: Greater than 6% improvement	Operating EPS of \$2.63, which was a 12.8% improvement	50%
Achievement of operating efficiency ratio objective	Minimum: Ratio of at least 66% Maximum: Ratio of less than 62%	Operating efficiency ratio of 58.7%	15%
Achievement of retail banking goals including indirect loan growth, achievement of budgeted non-interest income and organic growth in loans and deposits	Minimum: Achievement of one identified objective Maximum: Achievement of all four identified objectives	Achievement of three objectives	15%
Achievement of tactical objectives including effective integration of the Merchants merger, DFAST dry-run, IT enhancement initiatives and revenue earnings growth targets for NRS	Minimum: Achievement of two identified objectives Maximum:	Achievement of three objectives	10%

Achievement of commercial banking operating objectives including loan growth and related business deposits	Achievement of all five identified objectives Minimum: Achievement of one identified objective Maximum: Achievement of both identified objectives	Achievement of one objective.	7.5%
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Corporate Goal	Minimum Threshold and Maximum Achievement Levels	Achievement Level	2017 Achievement
Maintenance of asset quality metrics	Minimum: Net charge-off ratio of at least 0.40% Maximum: Net charge-off ratio of less than 0.20%	Net charge-off ratio of 0.18%	15%
Achievement of pre-tax earnings growth targets for financial services businesses	Minimum: Growth of less than 3% Maximum: Growth in excess of 10%	Growth of 26.5%	22.5%
Total Weighted Achievement Level			135%

For the 2017 MIP payments, which were paid in 2018, the following percentages of each named executive's base salaries were used to calculate the MIP payments: Mr. Tryniski 60%, Messrs. Kingsley, Donahue and Getman 40%, and Mr. Serbun 30%. Please see the Summary Compensation Table presented on page 30 and related footnotes for more information regarding the amount received by each of the named executives under the MIP.

The Compensation Committee has evaluated the MIP payments for the named executives for 2018, which will be paid in 2019, and has determined that the following percentage of each named executive's base salary will be used for the MIP calculation: Mr. Tryniski 70%, Messrs. Kingsley and Donahue 50%, Mr. Getman 40%, and Mr. Serbun 30%.

#### Equity-Based and Other Long-Term Incentive Compensation

The Compensation Committee believes that the interests of the Company's Shareholders are best served when a significant percentage of executive compensation is comprised of equity-based and other long-term incentives that appreciate in value contingent upon increases in the share price of the Company's stock and other indicators that reflect improvements in business fundamentals. Accordingly, in determining total compensation levels, the Compensation Committee includes annual grants of equity-based awards to the named executives (as presented on pages 26 to 27) and other key employees which are designed to accomplish long-term objectives of the Company's compensation program.

All equity grants are awarded under the 2014 Incentive Plan. The Company structures its equity program to provide that the named executives receive 75 percent of their target equity compensation on an annual basis (the "annual equity awards"); half of which is in the form of time vested stock options and half in the form of time vested restricted stock. The remaining 25 percent of the target award is granted every three years in the form of long-term performance-stock awards with vesting of these awards contingent upon achieving specific long-term market determined performance measures over a three year period (the "performance equity award").

The annual equity awards are awarded each year based on a combination of the Company's performance and individual performance determined by the Compensation Committee with the target level of such awards tied to the named executive's base salary and responsibilities. The annual equity awards vest pro rata over a five year period in order to encourage the executives to continue their service with the Company. With respect to the grant of equity awards to the named executives in 2017, the following percentage of each named executive's base salaries were used to calculate the equity grant: Mr. Tryniski 75%, Messrs. Kingsley, Donahue and Getman 55%, and Mr. Serbun 30%. Please see the Grants of Plan-Based Awards Table presented on page 31 and related footnotes for more information regarding the amount of stock options and restricted stock received by each of the named executives in connection with the annual equity awards.

The Compensation Committee has evaluated the annual equity grant awards for the named executives and has determined that the following percentage of each named executive's base salary will be used to determine the equity grants to be made in 2018: Mr. Tryniski 90%, Messrs. Kingsley and Donahue 60%, Mr. Getman 55%, and Mr. Serbun 30%.

The Company is precluded from repricing options or granting options retrospectively under its 2014 Incentive Plan. All grants to executive officers require the approval of the Compensation Committee. The Company's general practice is to grant equity awards only on the annual grant date, although there are

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occasions when grants have been made on other dates, such as the employment of new employees with grants being made as of the date of hire. The exercise price of the stock options is set at the fair market price of a share of the Company's common stock on the NYSE on the date of grant.

Please see the Summary Compensation Table and the Grants of Plan-Based Awards Table presented on pages 30 to 32 and the accompanying narrative disclosure for more information regarding the number and value of the stock option awards received by each of the named executives.

#### Three-Year Performance Equity Award (2016 – 2018)

In March 2016, the Committee granted a new long-term performance equity award to the named executives and senior management consisting of shares of performance restricted stock, the terms of which provide that between zero and 200% of the target award may be earned over the three-year performance period starting January 1, 2016 and ending December 31, 2018. The performance metric used to determine the level of achievement over the three-year performance period was based on the difference, measured in percentage points, between the Company's total shareholder return (stock price and dividends) and a benchmark total return index. The KBW Regional Banking Index (KRX) was selected again as the benchmark total return index because it was deemed to be an objective measure of the Company's performance and would provide a significant ongoing incentive to increase the long-term total returns for Shareholders.

#### Performance Levels Established by the Compensation Committee

Performance Measure	Threshold	Target	Maximum
Company annual Total Shareholder Return ("TSR") compared to benchmark KBW annual Total Shareholder Return ("KBW TSR") (both measured in terms of percentage point increase or decrease over the performance period)	Company TSR is less than KBW TSR by 5 percentage points or more annually, then the payment opportunity is zero.	Company TSR is equal to or within 1.99 percentage points annually of the KBW TSR, then the payment opportunity is 100% of Target Amount.	Company TSR exceeds the KBW TSR by 5 percentage points or more annually, then payment opportunity is 200% of Target Amount.

The Committee determined the target performance levels based on appropriate stretch performance goals taking into consideration the benchmark index, performance period, and range of performance measure criteria tied to the payout opportunity. The performance restricted stock award includes dividend equivalent right that will accrue, in the form of additional shares of common stock, if and only to the extent that the performance restricted stock is earned and vested at the end of the performance period. At the end of the three-year performance (December 31, 2018), the Compensation Committee will determine whether the achievement level is met, and at what level, under the performance measures for the long-term performance equity award.

#### Other Benefits

Although other personal benefits are not a key element of the Company's compensation program, the Company's named executives, along with certain other senior level executives, are provided a limited number of personal benefits whose purpose is to support those executives in their business functions. The Company provides the following benefits to the named executives, as quantified in the Summary Compensation Table:

- local club memberships to enable executives to interact and foster relationships with customers and the local business community. Memberships do not exceed \$10,250 for each named executive;
- a car allowance or use of a Company-owned vehicle for those executives responsible for managing geographic territories which span the Company's market from Northeastern Pennsylvania to the Canadian border and throughout Vermont and into Western Massachusetts; and
- group term life insurance coverage in excess of limits generally available to employees.



Please see the Summary Compensation Table and accompanying narrative disclosures presented on pages 30 to 31 for more information on personal benefits the Company provides to the named executives.

#### Retirement and Other Benefits

The Company provides retirement benefits through a combination of a Pension Plan and a 401(k) Plan for most of its regular employees, including the named executives. The 401(k) Plan and the Pension Plan are more fully described under the section entitled “Retirement Plan Benefits” on page 35. The Pension Plan is available to all of the Company’s employees after one year of service.

Certain named executives are also covered by an individual supplemental retirement agreement that generally provides for non-qualified retirement benefits that cannot be provided to the named executives under the Pension Plan due to Internal Revenue Code limitations. The Company’s supplemental retirement agreements are described under the section entitled “Retirement Plan Benefits.”

The Company offers the named executives and certain other senior level executives the ability to participate in the Deferred Compensation Plan for Certain Executive Employees of Community Bank System, Inc. (the “Deferred Compensation Plan”). The named executives may elect to defer cash compensation into the Deferred Compensation Plan as described under the section entitled “Nonqualified Deferred Compensation Plan.”

The Company has entered into an employment agreement with each of the named executives. These individual agreements generally provide for severance or other benefits following the termination, retirement, death or disability of the named executives. The agreements, which also include change in control provisions, are more fully described under the section entitled “Employment Agreements.” Such change in control provisions all contain a “double trigger,” providing benefits only upon a termination without cause or a termination for good reason in connection with a change in control and do not provide for any tax gross-ups payments upon a change in control event.

#### Succession Planning

The Company currently has a succession plan to help assure a smooth transition with respect to any changes that may occur in senior management. In the event of such changes, the Compensation Committee will consider appropriate transition agreements with key officers of the Company consistent with the purposes of the succession plan. The terms and conditions of any such transition agreements will be recommended by management and approved by the Compensation Committee.

#### Tax Considerations

Section 162(m) of the Internal Revenue Code (the “Code”) generally limits to \$1 million the tax deduction available to public companies for compensation paid to each the CEO and the three other most highly compensated executive officers, not including the CFO. Prior to the enactment of the Tax Cuts and Jobs Act in December 2017, certain types of compensation were deductible if the requirements of Section 162(m) of the Code with respect to performance-based compensation were satisfied. The Tax Cuts and Jobs Act generally amended Section 162(m) to eliminate the performance-based compensation exception and expand the pool of includable executive officers to include the CFO for 2018. The Compensation Committee considers the implications of Section 162(m) in structuring and managing executive compensation and generally intends to maximize the tax deductibility of compensation, while it retains discretion to structure executive compensation in the best overall interests of the Company and award compensation that exceeds deductibility limitations if deemed appropriate. As was the case prior to the enactment of the Tax Cut and Jobs Act, the Committee will continue to monitor issues concerning the deductibility of executive compensation. Because corporate objectives may not always be consistent with the requirements of tax deductibility, the Committee is prepared, when it deems it appropriate, to enter into compensation arrangements under which payments will not be deductible under Section 162(m). Thus, deductibility will be one of many factors considered by the Committee in ascertaining appropriate levels or modes of compensation.

#### Compensation Recovery

The Company has adopted a clawback policy which states that if a senior executive or other employee has engaged in fraud or intentional misconduct that caused or otherwise contributed to the need for a material restatement to the Company's financial results, the Board will determine whether the incentive-based compensation received by such executive or employee would have been lower based upon the restated results and it will seek recoupment of such overpayment to the extent permitted by applicable law. Any recoupment under the clawback policy may be in addition to any other disciplinary action the Board may determine, including the termination of employment.

#### Policy Regarding Derivatives, Pledging and Hedging

The Company has adopted a policy that prohibits all of its directors and employees, including the named executives, from engaging in short sale transactions, pledging shares on margin, trading in derivative securities of the Company's common stock, or engaging in the purchase or sale of any other financial instruments that are designed to hedge or offset any decrease in the market value of the Company's common stock.

#### COMPENSATION COMMITTEE REPORT

The Compensation Committee has reviewed and discussed the Compensation Discussion and Analysis with management. Based upon its review and discussion with management, the Compensation Committee has recommended to the Board that the Compensation Discussion and Analysis be included in this Proxy Statement and the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

Neil E. Fesette, Chair

Brian R. Ace

Mark J. Bolus

Raymond C. Pecor, III

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## Executive Compensation Disclosure Tables

The following table summarizes the compensation of the named executives for the fiscal years end December 31, 2017, 2016 and 2015. The named executives are the Company's CEO, CFO, and the three other most highly compensated executive officers ranked by their total compensation in the table below. The material terms of the employment, consulting and separation agreements with the named executives are set forth under the section entitled "Employment Agreements."

## SUMMARY COMPENSATION TABLE

for

Fiscal Years End December 31, 2017, 2016 and 2015

Name and Principal Position	Year	Salary (\$)	Stock Awards (\$)(1)	Option Awards (\$)(2)	Non-Equity Incentive Plan Compensation (\$)(3)	Change in Pension Value and Nonqualified Deferred Compensation Earnings (\$)(4)	All Other Compensation (\$)(5)	Total (\$)
Mark E. Tryniski President, Chief Executive Officer and Director	2017	\$ 750,704	\$ 214,600	\$ 215,279	\$ 619,993	\$ 1,274,728	\$ 32,730	\$ 3,108,034
	2016	\$ 744,937	\$ 679,665	\$ 228,073	\$ 402,267	\$ 551,240	\$ 32,026	\$ 2,638,208
	2015	\$ 725,000	\$ 204,381	\$ 200,258	\$ 445,875	\$ 781,612	\$ 33,868	\$ 2,390,994
Scott A. Kingsley Executive Vice President and Chief Financial Officer	2017	\$ 437,479	\$ 100,074	\$ 100,361	\$ 240,871	\$ 585,434	\$ 27,098	\$ 1,491,317
	2016	\$ 434,119	\$ 316,859	\$ 106,328	\$ 181,283	\$ 20,836	\$ 27,638	\$ 1,087,063
	2015	\$ 422,500	\$ 95,295	\$ 93,360	\$ 173,225	\$ 254,327	\$ 27,175	\$ 1,065,882
Brian D. Donahue Executive Vice President and Chief Banking Officer	2017	\$ 362,409	\$ 75,970	\$ 76,207	\$ 199,538	\$ 361,657	\$ 28,046	\$ 1,103,827
	2016	\$ 359,625	\$ 240,628	\$ 80,742	\$ 129,465	\$ 232,496	\$ 28,350	\$ 1,071,306
	2015	\$ 350,000	\$ 72,347	\$ 70,896	\$ 143,500	\$ 71,267	\$ 26,366	\$ 734,376
George J. Getman Executive Vice President and General Counsel	2017	\$ 388,295	\$ 81,396	\$ 81,651	\$ 213,791	\$ 544,240	\$ 23,719	\$ 1,333,092
	2016	\$ 385,312	\$ 257,794	\$ 86,510	\$ 163,713	\$ 2,302	\$ 25,720	\$ 921,351
	2015							