



Community Bank System, Inc.

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2005 First Quarter Report



Community Bank System, Inc.



Our Company generated a 19.5% increase in net income over the first quarter of 2004, exceeding \$13.3 million in a quarter for only the second time in our company's history. This increase was achieved via higher earning asset levels, increases from non-interest income sources (including securities gains), improved asset quality and lower acquisition expenses. Similarly, we achieved earnings per share (diluted) of \$0.43, up 13.2% from the \$0.38 we earned one year earlier, despite having 1.6 million, or 5.5%, greater shares outstanding. While these results are strong, on a linked quarter basis (compared to fourth quarter 2004), our increase was a far more modest 7.5%.

Also on a linked quarter basis, total loans were down 1%. Much of this can be linked to seasonality, as home and auto buying in our markets are historically at their lowest levels during the winter months. Our business lending also dipped from our fourth quarter 2004 level by 1.8%, although more than half of this decrease came from one \$8 million credit payoff from a single relationship in our Pennsylvania market. We remain very

optimistic about continued progress in our Pennsylvania markets, as evidenced by our recent de novo expansions there. We were also encouraged to see a noticeable up-tick in loan demand during the first few weeks of April, which replaces roughly a third of our first-quarter decline. In addition, our asset quality profile continued to improve and remains in a very favorable (in some cases, historically low) range.

Our net interest margin of 4.34% for the quarter continues to place us above peers, but reflects a 33-basis-point reduction from the first quarter of 2004. Earning asset yields were down 15 basis points from last year's first quarter, while the cost of funds increased 19 basis points, due principally to the effect of the seven rate hikes (25 basis points each) from the Federal Reserve since last June.

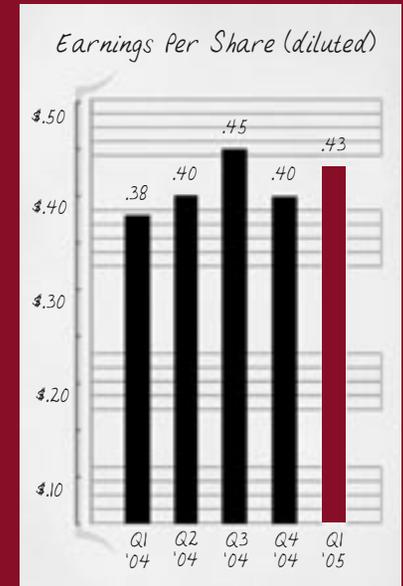
On a linked quarter basis, a portion of the 2% decline in net interest income was offset by improvements in select non-interest income components, an important strategic focus of ours over the past several years. Our employee benefits administration, consulting, and actuarial business continued to grow

at a double-digit pace, reaching a new quarterly high revenue mark by more than 20%. We also decided to take advantage of market conditions and sell certain investment securities in order to maximize their total return attributes, and shorten the average life of this portfolio. This decision generated more than \$1.7 million in gains in the quarter, or \$0.03 per share.

Lastly, our Board continues to focus on managing our capital effectively, authorizing in early April the repurchase of another 1.5 million common shares, or approximately 5% of total shares outstanding over the course of the next 20 months. As always, we continue to develop and evaluate both strategic and operational opportunities, in order to enhance revenues, control costs, and ultimately, increase our total return to shareholders.

Sincerely,

Sanford A. Belden,
President and Chief Executive Officer



Financial Highlights

	Three Months Ended Mar. 31, 2005	Three Months Ended Mar. 31, 2004	Three Months Ended March 31, 2005 Change from Mar. 31, 2004	Change from Dec. 31, 2004
<i>Income Statement Data (in thousands)</i>				
Net interest income	\$ 37,702	\$ 35,954	4.9%	-2.3%
Noninterest income*	12,959	10,530	23.1	19.6
Net income	\$ 13,334	\$ 11,155	19.5	5.3
Weighted avg. shares outstanding#	31,192	29,557	5.5%	-1.0%
<i>Common Per Share Data</i>				
Net income - diluted	\$ 0.43	\$ 0.38	13.2%	7.5%
Net income cash - diluted	0.47	0.41	14.6	6.8
Cash dividend declared	0.18	0.16	12.5	0.0
Period-end book value-stated	15.18	14.81	2.5	-2.0
Period-end book value-tangible	\$ 7.58	\$ 7.99	-5.1%	-4.1%
<i>End of Period Balance Sheet Data (in thousands)</i>				
Total assets	\$ 4,354,652	\$ 3,822,636	13.9%	-0.9%
Loans, net of unearned discount	2,334,385	2,105,415	10.9	-1.0
Deposits	2,976,953	2,740,933	8.6	1.6
Assets under management or administration	\$ 2,131,143	\$ 1,863,601	14.4%	1.4%

*Includes net securities gains/loses. #Reflects 2-1 stock split on 4/12/04.

Stock Performance

This table shows the high, low and closing price for CBU's common stock for each quarter.

Quarter Ending	Trade Price High	Trade Price Low	Closing Price	Volume
3/31/05	28.30	22.41	22.91	5,862,000
12/31/04	28.66	25.06	28.25	4,412,700
9/30/04	26.00	20.87	25.13	7,820,300
6/30/04	23.85	18.86	22.79	5,624,100
3/31/04	25.39	21.77	23.14	5,286,800

Investor Materials

Annual and quarterly shareholder reports, regulatory filings, press releases, and articles about the Corporation which have appeared in various publications are generally available in the "Investor Services" section of our Web site, www.communitybankna.com, or may be obtained from Ms. Josephine Anne E. Rurka by calling (315) 445-7300 or via e-mail at rurka@communitybankna.com.

Dividend Reinvestment and Stock Purchase Plan

The Corporation offers its shareholders a convenient and economical plan to increase their investment in Community Bank System, Inc. common stock. This plan provides a method of investing cash dividends and voluntary cash payments in additional shares of common stock without payment of brokerage commissions or service charges. Individuals who wish to purchase CBU stock for the first time may also participate in this plan. For additional information about the plan and a prospectus, please contact either:

American Stock Transfer & Trust Company
59 Maiden Lane
New York, NY 10038
www.investpower.com
Reinvestment questions: (800) 278-4353
General questions: (800) 937-5449
or

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