

COMMUNITY BANK SYSTEM, INC.

Form 424B3

February 10, 2017

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Registration No. 333-214961**

PROPOSED MERGER YOUR VOTE IS VERY IMPORTANT

Dear Stockholder:

On October 22, 2016, the board of directors of Merchants Bancshares, Inc. (Merchants) unanimously approved an Agreement and Plan of Merger (the Merger Agreement) between Merchants and Community Bank System, Inc. (Community Bank System). Merchants is holding a special meeting of stockholders on Thursday, March 23, 2017, at 10:00 a.m., Eastern time, at the DoubleTree by Hilton, 1117 Williston Road, South Burlington, Vermont 05403, for its stockholders of record on February 2, 2017, to vote on the proposals necessary to complete the merger. If Merchants stockholders adopt the Merger Agreement and the merger is subsequently completed, Merchants will merge with and into Community Bank System (the Merger), with Community Bank System continuing as the surviving company.

If the Merger Agreement proposal is approved and the Merger is subsequently completed, Merchants stockholders may elect to receive, in exchange for each outstanding share of Merchants common stock they hold, either: (i) \$40.00 in cash (which we refer to as the cash election consideration); (ii) 0.9630 shares of common stock of Community Bank System (which we refer to as the stock election consideration); or (iii) a combination of \$12.00 in cash and 0.6741 shares of common stock of Community Bank System (which we refer to as the mixed election consideration).

Both the cash election consideration and the stock election consideration are subject to proration and adjustment procedures to ensure that the total amount of cash paid, and the total number of shares of Community Bank System common stock issued, in the Merger to Merchants stockholders, as a whole, will equal as nearly as practicable the total amount of cash and number of shares that would have been paid and issued if all of the Merchants stockholders received the mixed election consideration. Merchants stockholders who fail to make a timely election or who make no election will receive the mixed election consideration. For more information, see Proposal I The Merger and The Merger Agreement.

The precise consideration that Merchants stockholders will receive if they elect the cash election consideration or the stock election consideration will not be known at the time that Merchants stockholders vote on the proposal to adopt the Merger Agreement or make an election as to the type of consideration that they would like to receive in the Merger. On October 21, 2016, which was the last trading date on the New York Stock Exchange (NYSE) preceding the public announcement of the Merger, the closing price of Community Bank System common stock was \$47.50 per share, valuing the mixed election consideration at approximately \$44.02 per share. On February 2, 2017, the most recent practicable date prior to the mailing of this Proxy Statement/Prospectus, the closing price of Community Bank System common stock on the NYSE was \$57.67, valuing the mixed election consideration at approximately \$50.88 per share. Based on 6,898,903 shares of Merchants common stock issued and outstanding, Community Bank System expects to issue in the Merger approximately 4,650,551 shares of its common stock before taking into account any adjustment for the issuance of cash in lieu of fractional shares.

The market prices of Community Bank System common stock and Merchants common stock will fluctuate before the completion of the Merger. **You should obtain current stock price quotations for Community Bank System and Merchants common stock before you vote.** Community Bank System common stock is listed on the NYSE under the symbol CBU. Merchants common stock is traded on the NASDAQ Global Select Market (NASDAQ) under the

symbol MBVT.

Under the terms of the Merger Agreement, in the event that the volume-weighted average trading price of Community Bank System common stock for a specified period prior to the closing is less than \$35.77 per share and the decrease in the price of Community Bank System's common stock is more than 20% greater than the decrease in the SNL Midcap U.S. Bank Index over the same period, Merchants has the right to terminate the Merger Agreement, Community Bank System has the option to increase the amount of Community Bank System common stock issuable to Merchants stockholders by a formula-based amount set forth in the Merger Agreement to prevent such termination.

The Merchants board of directors has unanimously determined that the Merger and the Merger Agreement are advisable and in the best interests of Merchants and its stockholders and unanimously recommends that you vote FOR the adoption of the Merger Agreement, FOR approval, on an advisory basis, of the Merger-related executive compensation payable to the Merchants named executive officers in connection with the Merger, and FOR the proposal to adjourn the Merchants special meeting, if necessary or appropriate, to solicit additional proxies in favor of the proposal to adopt the Merger Agreement.

The Merger cannot be completed unless at least two-thirds of the issued and outstanding shares of Merchants common stock entitled to vote at the special meeting vote in favor of the Merger. Whether or not you plan to attend the special meeting of stockholders, please take the time to vote by using the Internet, by telephone or by completing the enclosed proxy card and mailing it in the enclosed envelope. If you sign, date and mail your proxy card without indicating how you want to vote, your proxy will be counted as a vote FOR each of the proposals being voted on at Merchants' special meeting. If you fail to vote, or you do not instruct your broker how to vote any shares held for you in street name, it will have same effect as voting AGAINST the Merger Agreement, but it will have no impact on the advisory, non-binding proposal to approve the Merger-related executive compensation or the proposal to approve an adjournment of the special meeting.

The accompanying document is being delivered to Merchants stockholders as Community Bank System's Prospectus for its offering of Community Bank System common stock in connection with the Merger, and as Merchants' Proxy Statement for the solicitation of proxies for the special meeting.

This Proxy Statement/Prospectus provides you with detailed information about the proposed Merger. It also contains or references information about Merchants, Community Bank System and related matters. You are encouraged to read this document carefully. **In particular, you should read the Risk Factors section beginning on page 15 of this Proxy Statement/Prospectus for a discussion of the risks you should consider in evaluating the proposed Merger and how it will affect you.**

On behalf of our board of directors, I thank you for your prompt attention to this matter.

Sincerely,

Jeffrey L. Davis
Chairman of the Board of Directors

Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of the Merger, the issuance of the Community Bank System common stock in connection with the Merger or the other transactions described in this Proxy Statement/Prospectus, or passed upon the adequacy or accuracy of the disclosure in this document. Any representation to the contrary is a criminal offense.

The securities to be issued in connection with the Merger are not savings accounts, deposits or other obligations of any bank or savings association and are not insured by the Federal Deposit Insurance Corporation or any

other governmental agency.

This Proxy Statement/Prospectus is dated February 7, 2017, and is first being mailed to stockholders of Merchants on or about February 10, 2017.

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MERCHANTS BANCSHARES, INC.
275 Kennedy Drive
South Burlington, Vermont 05403

NOTICE OF SPECIAL MEETING OF STOCKHOLDERS TO BE HELD ON MARCH 23, 2017

NOTICE IS HEREBY GIVEN that a special meeting of the stockholders of Merchants Bancshares, Inc. (Merchants) will be held on Thursday, March 23, 2017, at 10:00 a.m., Eastern time, at the DoubleTree by Hilton, 1117 Williston Road, South Burlington, Vermont 05403, to consider and vote upon the following matters:

1. a proposal to adopt the Agreement and Plan of Merger, dated as of October 22, 2016, by and between Community Bank System, Inc. (Community Bank System) and Merchants (the Merger Agreement), which provides for the merger of Merchants with and into Community Bank System with Community Bank System as the surviving company (the Merger);
2. a non-binding, advisory proposal to approve the compensation payable to the named executive officers of Merchants in connection with the Merger (the Merger-Related Executive Compensation);
3. a proposal to approve one or more adjournments of the special meeting, if necessary or appropriate, to solicit additional proxies if there are insufficient votes at the time of the special meeting to adopt the Merger Agreement (the adjournment proposal); and
4. any other business which may properly come before the special meeting or any adjournment thereof.

The Merger is described in more detail in this Proxy Statement/Prospectus, which you should read carefully in its entirety before you vote. A copy of the Merger Agreement is attached as **Annex A** to this Proxy Statement/Prospectus. Only holders of record of Merchants common stock at the close of business on February 2, 2017 are entitled to notice of and to vote at the special meeting and any adjournments or postponements of the special meeting.

Under Delaware law, Merchants stockholders who do not vote in favor of adoption of the Merger Agreement will have the right to seek appraisal of the fair value of their Merchants common stock as determined by the Delaware Court of Chancery if the Merger is completed, but only if they submit a written demand for such an appraisal prior to the vote on adoption of the Merger Agreement and strictly comply with the other Delaware law procedures explained in this Proxy Statement/Prospectus. See the section entitled Proposal I The Merger Appraisal or Dissenters Rights beginning on page 58. The applicable Delaware law is reproduced in its entirety in Annex C to this Proxy Statement/Prospectus.

Please vote as soon as possible. The affirmative vote of two-thirds of the outstanding shares of Merchants common stock entitled to vote at the special meeting of stockholders is required for the adoption of the Merger Agreement. Approval of the non-binding, advisory Merger-Related Executive Compensation proposal requires the affirmative vote of a majority of the votes cast on the proposal. Approval of the adjournment proposal requires the affirmative vote of a majority of the votes cast on the proposal.

If you fail to vote, or you do not instruct your broker how to vote any shares held for you in street name, it will have same effect as voting AGAINST the Merger Agreement.

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To ensure your representation at the special meeting of stockholders, please follow the voting procedures described in the accompanying Proxy Statement/Prospectus and on the enclosed proxy card. This will not prevent you from voting in person, but it will help to secure a quorum and avoid added solicitation costs. Your proxy may be revoked at any time before it is voted by following the instructions provided in the Proxy Statement/Prospectus.

THE MERCHANTS BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT YOU VOTE FOR ALL PROPOSALS.

BY ORDER OF THE BOARD OF DIRECTORS

Jamie Oberle
Secretary

South Burlington, Vermont
February 7, 2017

YOUR VOTE IS IMPORTANT!

Whether or not you plan to attend the special meeting in person, Merchants urges you to submit your proxy as soon as possible by (1) calling the toll free telephone number specified on the enclosed proxy card, (2) accessing the Internet website specified on the enclosed proxy card, or (3) completing, signing and dating the enclosed proxy card and returning it in the postage paid envelope provided. If your shares are held in the name of a bank, broker or other fiduciary, please follow the instructions on the voting card provided by such entity.

If you have any questions concerning the Merger or other matters to be considered at the Merchants special meeting, would like additional copies of this Proxy Statement/Prospectus or need help voting your shares, please contact Innisfree M&A Incorporated, Merchants proxy solicitor, by calling (212) 750-5833.

PLEASE DO NOT SEND STOCK CERTIFICATES WITH THE PROXY CARD. YOU WILL BE SENT SEPARATE INSTRUCTIONS REGARDING MAKING ELECTIONS AS TO THE FORM OF MERGER CONSIDERATION YOU WOULD LIKE TO RECEIVE AND THE SURRENDER OF YOUR STOCK CERTIFICATES.

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QUESTIONS AND ANSWERS ABOUT THE MERGER

The following are answers to certain questions that you may have regarding the merger and the special meeting. We urge you to read carefully the remainder of this Proxy Statement/Prospectus because the information in this section may not provide all the information that might be important to you in determining how to vote. Additional important information is also contained in the annexes to, and the documents incorporated by reference in, this Proxy Statement/Prospectus.

Q: Why am I receiving this document?

Community Bank System, Inc. (Community Bank System) and Merchants Bancshares, Inc. (Merchants) have agreed to combine under the terms of an Agreement and Plan of Merger by and between Community Bank System and Merchants, dated as of October 22, 2016 (the Merger Agreement), that is described in this Proxy Statement/Prospectus. A copy of the Merger Agreement is attached to this Proxy Statement/Prospectus as **Annex A**. In order to complete the merger of Merchants with and into Community Bank System (the Merger), the stockholders of Merchants must vote to adopt the Merger Agreement. Merchants will hold a special meeting of its stockholders to solicit this approval, as well as the non-binding advisory approval of the Merger-Related Executive Compensation and, if necessary, the approval of the adjournment proposal. We are delivering this Proxy Statement/Prospectus to you as both a Proxy Statement of Merchants and a Prospectus of Community Bank System. It is a Proxy Statement because the Merchants board of directors is soliciting proxies from its stockholders. It is a Prospectus because Community Bank System will issue Community Bank System common stock to the Merchants stockholders who receive stock consideration in the Merger, and this Prospectus contains information about Community Bank System common stock. This Proxy Statement/Prospectus contains important information about the Merger, the Merger Agreement, the special meeting of Merchants stockholders, and other related matters, and we encourage you to read it carefully.

Q: What will happen to Merchants as a result of the Merger?

If the Merger is completed, Merchants will cease to exist and Merchants Bank, the wholly-owned subsidiary of Merchants, will become a direct, wholly-owned subsidiary of Community Bank System. Immediately following completion of the Merger, Merchants Bank will then merge with and into Community Bank, N.A. (Community Bank), the wholly-owned subsidiary of Community Bank System, with Community Bank being the surviving bank.

Q: Who is being asked to approve matters in connection with the Merger?

Only Merchants stockholders are being asked to vote to approve the Merger-related proposals. Community Bank System is not required to obtain Community Bank System stockholder approval of the Merger or the Merger Agreement.

Q: What will I receive in the Merger?

If the Merger Agreement proposal is approved and the Merger is subsequently completed, each outstanding share of Merchants common stock will be converted into the right to receive either:

\$40.00 in cash, without interest (the cash election consideration);
0.9630 shares of Community Bank System common stock, plus cash in lieu of fractional shares (the stock election consideration); or
a combination of both \$12.00 in cash and 0.6741 shares of Community Bank System common stock, plus cash in lieu of fractional shares (the mixed election consideration).

The above consideration is subject to proration procedures that are designed to ensure that the total amount of cash paid, and the total number of shares of Community Bank System common stock issued, in the Merger will equal as nearly as practicable the total amount of cash and number of shares that would have been paid and issued if all of the Merchants stockholders received the mixed election consideration.

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You may elect to receive the cash election consideration, the stock election consideration, or the mixed election consideration. However, the ability to receive the consideration of your choice will depend on the elections of other Merchants stockholders. The proration of the consideration payable to Merchants stockholders in the Merger will not be known until Community Bank System tallies the results of the elections made by Merchants stockholders, which will not occur until near or after the closing of the Merger.

Q: Will I receive the form of consideration that I elect?

A: If you elect to receive the mixed election consideration, you will receive the mixed election consideration. If you elect to receive the cash election consideration or stock election consideration, you may not receive the exact form of consideration that you elect. If you make no election with respect to your shares of Merchants common stock (and do not exercise appraisal rights), you will receive the mixed election consideration.

It is currently estimated that, if the Merger is completed, Community Bank System will issue, in the aggregate, approximately 4.65 million shares of Community Bank System common stock and pay approximately \$82.78 million in cash to Merchants stockholders. Under the proration procedures in the Merger Agreement, the total amount of cash paid, and the total number of shares of Community Bank System common stock issued, in the Merger to the holders of shares of Merchants common stock (other than excluded shares), as a whole, will equal as nearly as practicable the total amount of cash and number of shares that would have been paid and issued if all of such shares of Merchants common stock were converted into the mixed election consideration.

Whether you receive the amount of cash and/or stock you request in your election form will depend in part on the elections of other Merchants stockholders. You may not receive the form of consideration that you elect in the Merger, and you may instead receive a pro-rata amount of cash and/or Community Bank System common stock.

The greater the oversubscription of the stock election consideration, the less stock and more cash a Merchants stockholder making the stock election will receive. Reciprocally, the greater the oversubscription of the cash election consideration, the less cash and more stock a Merchants stockholder making the cash election will receive. However, in no event will a Merchants stockholder who makes the cash election or the stock election receive less cash and more shares of Community Bank System common stock, or fewer shares of Community Bank System common stock and more cash, respectively, than a stockholder who elects the mixed election consideration. See The Merger Agreement Election and Proration Procedures beginning on page 63 of this Proxy Statement/Prospectus.

The proration of the consideration payable to Merchants stockholders who elect to receive the cash election consideration and/or the stock election consideration will not be known until Community Bank System tallies the results of the elections, which will not occur until near or after the closing of the Merger.

Q: How will Merchants stock options be treated in the Merger?

A: Each Merchants stock option outstanding and unexercised immediately prior to the effective time of the Merger, whether or not then vested or exercisable, will be cancelled and automatically converted into the right to receive a cash amount equal to the aggregate number of Merchants shares subject to such option *multiplied by* the excess of the value of the mixed election consideration over the exercise price of such option.

Q: How will shares of Merchants common stock subject to vesting or forfeiture restrictions be treated in the Merger?

Each share of Merchants common stock subject to vesting or forfeiture restrictions and granted under any Merchants benefit plan that is outstanding immediately prior to the effective time, whether or not then vested, will automatically vest in full, and any restrictions thereon will lapse, and such

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stock will be converted into the right to receive an amount of cash equal to the value of the mixed election consideration plus dividends, if any, accrued but unpaid as of the effective time with respect to such restricted share.

Q: How will warrants to purchase Merchants common stock be treated in the Merger?

A: Each warrant that was originally issued on April 25, 2008 by NUVO Bank & Trust Company (with respect to which Merchants issued replacement warrants on December 4, 2015), which we refer to as organizers warrants, to purchase Merchants common stock outstanding as of the effective time will be converted at the effective time into a warrant to acquire, upon payment of the amount determined by dividing the per share exercise price immediately prior to the effective time by the stock election consideration of 0.9630, the number of shares of Community Bank System common stock determined by *multiplying* (i) the number of shares of Merchants common stock which may be acquired upon exercise of such organizers warrant immediately prior to the effective time by (ii) the stock election consideration of 0.9630.

Each warrant that was originally issued on April 30, 2013 by NUVO Bank & Trust Company (with respect to which Merchants issued replacement warrants on December 4, 2015), which we refer to as 2013 warrants, to purchase Merchants common stock outstanding as of the effective time will be converted into the right to receive, at the holder's election, either (i) a cash payment in cancellation of such 2013 warrant equal to the number of shares of Merchants common stock which may be acquired upon exercise of such 2013 warrant *multiplied by* the excess, if any, of the cash election consideration of \$40.00 over the per share 2013 warrant exercise price immediately prior to the effective time or (ii) a replacement 2013 warrant certificate issued by Community Bank System and representing the right to acquire prior to the expiration date of the original 2013 warrant,