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

FORM 10-Q/A
Amendment No. 2

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2007

001-11663
(Commission File Number)

COMMUNITY BANKS, INC.
(Exact name of registrant as specified in its charter)

PENNSYLVANIA	**23-2251762**
(State of incorporation)	**(I.R.S. Employer Identification Number)**
777 East Park Dr., Harrisburg, PA	**17111**
(Address of principal executive offices)	**(Zip Code)**

(717) 920-5800
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Sections 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days.
Yes __X__ No _____

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act. (Check one):
Large accelerated filer _____ Accelerated filer __X__ Non-accelerated filer _____

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).
Yes _____ No __X__

The number of shares of the registrant's common stock, $5.00 par value, outstanding as of April 30, 2007 was 24,751,204.

EXPLANATORY NOTE REGARDING THIS FORM 10-Q/A – AMENDMENT No. 2

On June 21, 2007, Community Banks, Inc. ("Community") filed Form 10-Q/A – Amendment No. 1 to amend our Form 10-Q for the three months ended March 31, 2007, initially filed with the Securities and Exchange Commission on May 10, 2007 ("the original Form 10-Q").

As described in its Current Report on Form 8-K filed on June 18, 2007, and as discussed in Note 2 to the Consolidated Financial Statements included herein, Community filed Amendment No. 1 to its original Form 10-Q to amend and restate its financial statements and other financial information as a result of Community's decision to reverse its application of Statement of Financial Accounting Standards No. 159, "*The Fair Value Option for Financial Assets and Liabilities*" (SFAS No. 159) with respect to certain investment securities.

Subsequent to the filing of the Form 10-Q/A - Amendment No. 1 on June 21, 2007, Community discovered the omission of a table in Management's Discussion and Analysis. This Form 10-Q/A – Amendment No.2 is filed to include the omitted table, which now appears on page 19 of this document.

Both Form 10-Q/A - Amendment No. 1 and this Form 10-Q/A – Amendment No. 2 have been presented as of the date of the original Form 10-Q and the disclosures contained herein have not been updated for presentation as of any later date. Information not directly affected by the reversal of the application of SFAS No. 159 remains substantially unchanged in both Amendment No. 1 and Amendment No.2 and continues to reflect the disclosures made at the time of the original filing.

For convenience, the entire Quarterly Report on Form 10-Q for the three months ended March 31, 2007 has been re-filed in this Form 10-Q/A – Amendment No. 2. Pursuant to SEC Rule 12b-15, Community is filing updated exhibits 31.1, 31.2, and 32 in connection with this filing.

COMMUNITY BANKS, INC. AND SUBSIDIARIES
FORM 10-Q/A – Amendment No. 2
INDEX

PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

Community Banks, Inc. and Subsidiaries
CONSOLIDATED INTERIM BALANCE SHEETS
(Dollars in thousands except per share data)

	March 31, 2007 (Restated)	December 31, 2006
ASSETS		
Cash and due from banks	$ 70,128	$ 73,608
Federal funds sold	10,199	---
Cash and cash equivalents	80,327	73,608
Interest-bearing deposits in other banks	32,964	3,561
Investment securities, available for sale	645,054	636,066
Investment securities, held to maturity (fair value approximates $23,353 and $23,415)	23,080	23,070
Loans, net of allowance for loan losses of $24,379 and $23,626	2,417,939	2,347,263
Premises and equipment, net	46,261	46,335
Goodwill and other intangible assets	258,812	259,406
Accrued interest receivable and other assets	123,302	107,061
Total assets	$ 3,627,739	$ 3,496,370
LIABILITIES		
Deposits		
Non-interest bearing	$ 367,917	$ 368,329
Interest bearing	2,161,270	2,144,853
Total deposits	2,529,187	2,513,182
Short-term borrowings	67,747	108,927
Long-term debt	438,196	315,079
Subordinated debt	72,167	51,548
Accrued interest payable and other liabilities	29,878	21,473
Total liabilities	3,137,175	3,010,209
STOCKHOLDERS' EQUITY		
Preferred stock, no par value; 500,000 shares authorized; no shares issued and outstanding	---	---
Common stock, $5.00 par value; 50,000,000 shares authorized; 24,478,000 shares issued	122,391	122,391
Surplus	373,335	373,142
Retained Earnings	18,646	17,609
Accumulated other comprehensive income (loss), net of tax	650	(1,806)
Treasury stock; 933,000 and 959,000 shares, at cost	(24,458)	(25,175)
Total stockholders' equity	490,564	486,161
Total liabilities and stockholders' equity	$ 3,627,739	$ 3,496,370

The accompanying notes are an integral part of the consolidated interim financial statements.

Community Banks, Inc. and Subsidiaries
CONSOLIDATED INTERIM STATEMENTS OF INCOME
(Dollars in thousands except per share data)

	Three Months Ended March 31, 2007 (Restated)	Three Months Ended March 31, 2006
INTEREST INCOME:		
Loans, including fees	$ 43,520	$ 39,101
Investment securities:		
Taxable	5,400	4,413
Tax exempt	2,632	2,368
Dividends	552	614
Other	135	393
Total interest income	52,239	46,889
INTEREST EXPENSE:		
Deposits	18,886	13,421
Short-term borrowings	1,564	696
Long-term debt	4,500	5,111
Subordinated debt	1,022	797
Total interest expense	25,972	20,025
Net interest income	26,267	26,864
Provision for loan losses	1,300	500
Net interest income after provision for loan losses	24,967	26,364
NON-INTEREST INCOME:		
Investment management and trust services	1,445	1,013
Service charges on deposit accounts	2,996	2,531
Other service charges, commissions and fees	2,028	1,700
Insurance premium income and commissions	1,176	928
Mortgage banking activities	548	468
Earnings on investment in life insurance	688	656
Investment security gains	2	283
Other than temporary impairment of investment securities (see Note 2)	(4,390)	---
Other	591	805
Total non-interest income	5,084	8,384
NON-INTEREST EXPENSES:		
Salaries and employee benefits	12,009	11,418
Net occupancy and equipment expense	3,794	3,512
Marketing expense	505	575
Telecommunications expense	525	551
Amortization of intangibles	661	654
Other	4,647	3,823
Total non-interest expenses	22,141	20,533
Income before income taxes	7,910	14,215
Income taxes	1,323	3,646
Net income	$ 6,587	$ 10,569
CONSOLIDATED PER SHARE DATA		
Basic earnings per share	$ 0.28	$ 0.44
Diluted earnings per share	$ 0.28	$ 0.44
Dividends declared	$ 0.21	$ 0.19

The accompanying notes are an integral part of the consolidated interim financial statements.

Community Banks, Inc. and Subsidiaries
CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
For the Three Months Ended March 31, 2007 and 2006
(Dollars in Thousands)

	Outstanding Shares	Common Stock	Surplus	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Equity
Balance, January 1, 2006	22,915	$ 116,572	$ 347,827	$ 27,031	$ (3,779)	$ (10,978)	$ 476,673
Comprehensive income:							
Net income				10,569			10,569
Unrealized loss on securities, net of reclassification adjustment and tax effect					(589)		(589)
Total comprehensive income							9,980
Cash dividends ($0.19 per share)				(4,545)			(4,545)
5% stock dividend	1,133	5,820	24,162	(29,982)			---
Purchases of treasury stock	(264)					(7,349)	(7,349)
Exercise of common stock options and issuances under stock purchase plan	47			(653)		1,292	639
Compensation and tax benefits from employee stock transactions			189				189
Balance, March 31, 2006	23,831	$ 122,392	$ 372,178	$ 2,420	$ (4,368)	$ (17,035)	$ 475,587
Balance, January 1, 2007	23,519	$ 122,391	$ 373,142	$ 17,609	$ (1,806)	$ (25,175)	$ 486,161
Comprehensive income:							
Restated net income				6,587			6,587
Restated unrealized gain on securities, net of reclassification adjustment and tax effect					2,456		2,456
Total comprehensive income							9,043
Cash dividends ($0.21 per share)				(4,944)			(4,944)
Purchases of treasury stock	(12)					(298)	(298)
Exercise of common stock options and issuances under stock purchase plan	38			(606)		1,015	409
Compensation and tax benefits from employee stock transactions			193				193
Balance, March 31, 2007	23,545	$ 122,391	$ 373,335	$ 18,646	$ 650	$ (24,458)	$ 490,564

The accompanying notes are an integral part of the consolidated interim financial statements.

Community Banks, Inc. and Subsidiaries
CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS
(Dollars in thousands)

	Three Months Ended March 31, 2007 (Restated)	Three Months Ended March 31, 2006
Operating Activities:		
Net income	$ 6,587	$ 10,569
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for loan losses	1,300	500
Depreciation and amortization	1,830	1,817
Stock option expense	193	118
Net amortization (accretion) of securities	11	144
Realized gains on sales of available-for-sale securities, net	(2)	(283)
Other than temporary impairment of investment securities	4,390	---
Loans originated for sale	(7,178)	(1,335)
Proceeds from sales of loans held for sale	5,813	711
Gains on loan sales	(584)	(14)
Earnings on investment in life insurance	(688)	(656)
Net change in other assets and liabilities, net	(8,547)	9,384
Net cash provided by operating activities	3,125	20,955
Investing Activities:		
Net change in interest-bearing deposits in other banks	(29,403)	(71,447)
Activity in available-for-sale securities:		
Sales	33,313	38,557
Maturities, prepayments and calls	19,400	13,030
Purchases	(62,295)	(12,593)
Net increase in total loans	(71,493)	(49,726)
Proceeds from sale of loans	1,441	---
Additions to premises and equipment	(1,096)	(1,261)
Net cash used in investing activities	(110,133)	(83,440)
Financing Activities:		
Net increase in deposits	16,005	79,498
Net change in short-term borrowings	(41,180)	(32,249)
Proceeds from issuance of long-term debt	145,619	75,620
Repayment of long-term debt	(1,884)	(42,444)
Cash dividends and cash paid in lieu of fractional shares	(4,944)	(4,545)
Purchases of treasury stock	(298)	(7,349)
Tax benefits from employee stock transactions	---	71
Proceeds from issuance of common stock	409	639
Net cash provided by financing activities	113,727	69,241
Net change in cash and cash equivalents	6,719	6,756
Cash and cash equivalents at beginning of period	73,608	76,820
Cash and cash equivalents at end of period	$ 80,327	$ 83,576

The accompanying notes are an integral part of the consolidated interim financial statements.

1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Community Banks, Inc. and Subsidiaries ("Community") have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included.

Operating results for the three months ended March 31, 2007, are not necessarily indicative of the results that may be expected for the year ending December 31, 2007.

For further information, refer to the audited consolidated financial statements, and footnotes thereto, included in the Annual Report on Form 10-K, for the year ended December 31, 2006.

Community is a financial holding company whose wholly-owned subsidiaries include CommunityBanks, CommunityBanks Investments, Inc. (CBII), and Community Banks Life Insurance Co. (CBLIC). CommunityBanks provides a wide range of services through its network of offices in Adams, Berks, Chester, Cumberland, Dauphin, Lancaster, Luzerne, Northumberland, Schuylkill, Snyder, and York Counties in Pennsylvania and Carroll County in Maryland.

2. Restatement and Fair Value Measurements

In September 2006, the Financial Accountings Standard Board ("FASB") issued SFAS No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for measuring fair value, and enhances disclosures about assets and liabilities carried at fair value, but does not change existing guidance as to whether or not an asset or liability is carried at fair value. SFAS No. 157 also: (1) precludes the use of a liquidity or block discount when measuring instruments traded in an active market at fair value; (2) requires cost related to acquiring financial instruments carried at fair value to be included in earnings and; (3) clarifies that an issuer's credit standing should be considered when measuring liabilities at fair value. The purpose of this Standard was to provide consistency and comparability in determining fair value measurements.

In February 2007, the FASB issued Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* ("SFAS No. 159"), which permits certain financial assets and financial liabilities to be measured at fair value, using an instrument-by-instrument election. The initial effect of adoption of SFAS No. 159 is required to be accounted for as a cumulative-effect adjustment to opening retained earnings for the year in which SFAS No. 159 is applied. Retrospective application of SFAS No. 159 to years preceding the effective date is not permitted.

Under the early adoption provisions of both Standards, Community elected to adopt SFAS No. 157 and SFAS No. 159 as of January 1, 2007. In its original filing on Form 10-Q, Community applied the fair value option provisions of SFAS No. 159 to certain securities that had a fair value of approximately $150.2 million that were included in its available-for-sale portfolio at December 31, 2006. These securities, which had an historical cost basis of approximately $154.9 million, consisted primarily of various mortgage-backed securities and collateralized mortgage backed obligations. Effective January 1, 2007, these securities were transferred to trading assets at their then fair value. Early adoption was elected to accommodate various aspects of Community's liquidity, interest rate risk, and asset liability management processes by extending portfolio duration and reducing call and prepayment risk. Additionally, the adoption was designed to provide an ongoing process designed to facilitate funding for Community's future acquisition strategies.

2. Restatement and Fair Value Measurements (continued)

The transfer of these securities from available-for-sale portfolio to trading assets after the early adoption of SFAS No. 159 resulted in a one-time cumulative after-tax charge of $3.1 million ($4.7 million pre-tax) to opening retained earnings as of January 1, 2007. All of the available-for-sale securities for which SFAS No. 159 was adopted reflected previously unrecognized loss positions prior to January 1, 2007 (i.e., their fair value was less than historic cost). Prior to the decision to early adopt SFAS No. 159 for the identified securities, Community had intended to hold these securities until their scheduled maturity or until there was a recovery in the market prices associated with these specific investments.

Subsequent to the first quarter of 2007, Community sold these trading securities, all of which had been reclassified pursuant to the early adoption of SFAS No. 159, in order to facilitate a balance sheet restructuring strategy. The securities that were sold had a duration of 3.4 years and an average yield of 4.50% The proceeds of the sale were utilized to facilitate the acquisition of $148 million of replacement investments with an average yield of 5.47% and a duration of 4.2 years. A portion of these replacement investments, approximately $20 million, were classified as trading securities. The remaining replacement investments, totaling approximately $128 million were classified as available-for sale securities at the date of purchase. The sale and reinvestment of sale proceeds pursuant to the balance sheet restructuring will result in an annual improvement in net interest income of nearly $1.4 million on a pre-tax basis over the replacement duration of 4.2 years.

Subsequent to both the transactions discussed above and the original filing of Community's first quarter Form 10-Q on May 10 2007, the staff of the Securities and Exchange Commission (SEC) advised Community that the balance sheet restructuring strategy, as presented, was inconsistent with the spirit and intent of SFAS No. 159 and therefore was deemed a non-substantive adoption of the Standard. Based on discussions with the staff, it was determined that failure to reclassify all of the replacement securities as trading assets would require a reversal of Community's decision to apply the fair value option to the $150.2 million of investment securities that had been included in its available-for-sale portfolio as of December 31, 2006. Consequently, Community decided to reverse its decision to apply SFAS No. 159 to those securities as of January 1, 2007. Based upon Community's understanding of the views of the SEC, the investment securities that were subsequently sold early in the second quarter and that were originally reported as trading assets at March 31, 2007, are to be reclassified as available-for-sale securities. Furthermore, those securities are to be considered "other-than-temporarily-impaired" at the end of the first quarter of 2007 based upon the presumption that Community had the intent to sell those securities as of March 31, 2007. Accordingly, as part of this restatement, Community has recognized a charge to earnings for the other-than-temporary impairment of $4.4 million for the first quarter of 2007 and has reversed the after-tax charge of $3.1 million ($4.7 million pre-tax) to opening retained earnings as of January 1, 2007. The effect of the other-than-temporary impairment charge and other related adjustments reduced income before income taxes by $4.7 million, reduced income tax expense by $1.6 million, and reduced net income by $3.1 million for the three months ended March 31, 2007. In the aggregate, these changes resulted in restated net income of $6.6 million, or $0.28 per share.

Community Banks, Inc. and Subsidiaries
NOTES TO CONSOLIDATED INTERIM FINANCIAL STATEMENTS
(Unaudited)

2. Restatement and Fair Value Measurements (continued)

The following table reflects the previously reported and the restated amounts as of and for the three months ended March 31, 2007 (in thousands, except share data):

	As of and for the Three Months Ended March 31, 2007	
	Previously reported	Restated
Consolidated Interim Balance Sheet Data:		
Trading assets	$ 146,094	$ ---
Investment securities, available for sale	499,747	645,054
Accrued interest receivable and other assets	124,162	123,302
Total assets	3,629,386	3,627,739
Accrued interest payable and other liabilities	31,525	29,878
Total liabilities	3,138,822	3,137,175
Total liabilities and stockholders' equity	3,629,386	3,627,739
Consolidated Interim Statement of Income:		
Interest income on taxable investment securities	3,701	5,400
Interest income on trading account securities	1,869	---
Total interest income	52,409	52,239
Net interest income	26,437	26,267
Net interest income after provision for loan losses	25,137	24,967
Trading activities gain	146	---
Other than temporary impairment of investment securities	---	(4,390)
Total non-interest income	9,620	5,084
Income before income taxes	12,616	7,910
Income taxes	2,970	1,323
Net income	9,646	6,587
Consolidated Interim Statement of Changes in Stockholders' Equity		
Unrealized gain (loss) on securities, net of reclassification adjustment and tax effect	(603)	2,456
Consolidated Interim Statement of Cash Flows		
Net income	9,646	6,587
Net amortization (accretion) of securities	(41)	11
Other than temporary impairment of investment securities	---	4,390
Net change in fair value of trading assets	(312)	---
Net change in other assets and liabilities, net	(6,852)	(8,547)
Maturities and prepayments in trading assets	5,171	---
Maturities, prepayments and calls (in available-for-sale securities)	14,229	19,400
Consolidated Per Share Data:		
Basic earnings per share	$ 0.41	$ 0.28
Diluted earnings per share	$ 0.41	$ 0.28

2. Restatement and Fair Value Measurements (continued)

Community's early adoption SFAS No. 157, among other things, requires enhanced disclosures about assets and liabilities that are carried at fair value. SFAS No. 157 establishes a hierarchal disclosure framework associated with the level of pricing observability utilized in measuring assets and liabilities at fair value. The three broad levels defined by the SFAS No. 157 hierarchy are as follows:

Level I – Quoted prices are available in active markets for identical assets or liabilities as of the reported date.

Level II – Pricing inputs are other than quoted prices in active markets, which are either directly or indirectly observable as of the reported date. The nature of these assets and liabilities include items for which quoted prices are available but traded less frequently, and items that are fair valued using other financial instruments, the parameters of which can be directly observed.

Level III – Assets and liabilities that have little to no pricing observability as of the reported date. These items do not have two-way markets and are measured using management's best estimate of fair value, where the inputs into the determination of fair value require significant management judgment or estimation.

The following table summarizes the valuation of Community's available-for-sale securities that Community measures at fair value on a recurring basis, by the above SFAS No. 157 pricing observability levels as of March 31, 2007, (in thousands):

Description	Level I	Level II	Total
Available-for-sale securities	$145,307	$499,747	$645,054

3. Summary of Significant Accounting Policies

Earnings Per Share **-** Basic earnings per share represents income available to common stockholders divided by the weighted-average number of common shares outstanding during the period. Diluted earnings per share reflect additional common shares that would have been outstanding if dilutive potential common shares had been issued, as well as any adjustment to income that would result from the assumed issuance. Potential common shares that may be issued by Community relate solely to outstanding stock options, and are determined using the treasury stock method. All share and per share amounts are restated for stock splits and stock dividends that occur prior to the issuance of the financial statements.

Earnings per share for the three months ended March 31 have been computed as follows (in thousands, except share data):

	Three Months Ended March 31,	
	2007 (Restated)	**2006**
Net income	$ 6,587	$ 10,569
Weighted average shares outstanding (basic)	23,535	23,974
Effect of dilutive stock options	148	215
Weighted average shares outstanding (diluted)	23,683	24,189
Per share information:		
Basic earnings per share	$ 0.28	$ 0.44
Diluted earnings per share	0.28	0.44

3. Summary of Significant Accounting Policies (continued)

Comprehensive Income (Loss) **-** The components of comprehensive income (loss) and related tax effect for the three months ended March 31 are as follows (in thousands):

	Three Months Ended March 31, 2007 (Restated)	Three Months Ended March 31, 2006
Unrealized holding losses on available-for-sale securities	$ (610)	$ (623)
Reclassification adjustments for net (gains) losses included in net income	4,388	(283)
Net unrealized gains (losses)	3,778	(906)
Tax effect	(1,322)	317
Net-of-tax amount	$ 2,456	$ (589)

The components of accumulated other comprehensive income (loss), included in stockholders' equity, are as follows (in thousands):

	March 31, 2007	December 31, 2006
Net unrealized gain on available-for-sale securities	$ 4,212	$ 434
Tax effect	(1,474)	(152)
Net-of-tax amount	2,738	282
Underfunded pension liability	(3,213)	(3,213)
Tax effect	1,125	1,125
Net-of-tax amount	(2,088)	(2,088)
Accumulated other comprehensive income (loss)	$ 650	$ (1,806)

Accounting Developments –

FIN 48 – In July 2006, the FASB issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN No. 48"), which sets out a framework for preparers to use to determine the appropriate level of tax reserves to maintain for uncertain tax positions. Community adopted FIN No. 48 on January 1, 2007, with no effect to the consolidated financial statements.

EITF 06-11 - In March 2007, FASB ratified Emerging Issues Task Force ("EITF") Issue No. 06-11, "Accounting for Income Tax Benefits of Dividends on Share-Based Payment Awards." EITF 06-11 requires companies to recognize the income tax benefit realized from dividends or dividend equivalents that are charged to retained earnings and paid to employees for nonvested equity-classified employee share-based payment awards as an increase to additional paid-in capital. EITF 06-11 is effective for fiscal years beginning after September 15, 2007. Community does not expect that EITF 06-11 will have a material impact on its financial position, results of operations or cash flows.

EITF 06-10 - In March 2007, the FASB ratified EITF Issue No. 06-10 "Accounting for Collateral Assignment Split-Dollar Life Insurance Agreements". EITF 06-10 provides guidance for determining a liability for the postretirement benefit obligation as well as recognition and measurement of the associated asset on the basis of the terms of the collateral assignment agreement. EITF 06-10 is effective for fiscal years beginning after December 15, 2007. Community is currently assessing the impact of EITF 06-10 on its consolidated financial position and results of operations.

4. Subsequent Event / Pending Merger:

On May 1, 2007, Community announced that it had signed a definitive agreement pursuant to which Community will combine with Susquehanna Bancshares, Inc. ("Susquehanna"), under Susquehanna's charter. Under the terms of the agreement, each Community shareholder will be entitled to elect to receive for each share of Community stock they own, either $34.00 in cash or 1.48 shares of Susquehanna common stock. Community shareholders may elect to receive cash for some shares and stock for others, but all shareholder elections will be subject to allocation procedures that will result in the exchange of 90 percent of Community's common shares outstanding for shares of Susquehanna common stock and the remaining 10 percent of Community common shares outstanding for cash. At the time of the announcement, the value of the transaction was approximately $860 million. Following consummation, the joint franchise will include approximately 240 banking offices in the mid-Atlantic region. The merger is subject to regulatory approval and the separate approvals of the shareholders of both Community and Susquehanna.

5. Subsequent Event / Acquisitions:

On April 1, 2007, Community and BUCS Financial Corp ("BUCS"), parent company of BUCS Federal Bank, completed a merger in which BUCS was merged into Community. Also on that date, BUCS Federal Bank was merged into CommunityBanks, Community's banking subsidiary. BUCS was headquartered in Baltimore County, Maryland, with 4 banking offices in Baltimore and Howard counties, Maryland. Management expects the merger will enhance Community's banking franchise by expanding its presence in desirable Maryland markets.

The purchase price was paid in shares of Community common stock (65%) and cash (35%). Electing BUCS shareholders received 0.99 shares of Community in exchange for each share of BUCS common stock and cash in lieu of fractional shares. Community issued approximately 550,000 shares at an aggregate value of approximately $13 million, based on Community's share price of $23.87 at the merger date. Cash payments to electing BUCS shareholders totaled $7.1 million. Option holders of BUCS common stock were paid an aggregate $1.4 million, representing the per-share amount equal to the difference between $24.00 and the exercise price of their options, and their options were canceled. BUCS had approximately $145 million in assets, $120 million in net loans, $9 million in investments, $121 million in deposits, $13 million in borrowings and $10 million of stockholders' equity at the merger date.

On April 1, 2007, Community and East Prospect State Bank ("East Prospect") completed a merger in which East Prospect was merged into CommunityBanks. East Prospect was single-branch bank located in York County, Pennsylvania. Management expects the merger will enhance Community's banking franchise by adding to its presence in York County.

The purchase price was paid in shares of Community common stock (75%) and cash (25%). Electing East Prospect shareholders received 23.4 shares of Community in exchange for each share of East Prospect common stock and cash in lieu of fractional shares. Community issued approximately 668,000 shares at an aggregate value of approximately $16 million, based on Community's share price of $23.87 at the merger date. Cash payments to electing East Prospect shareholders totaled $5.4 million. East Prospect had approximately $57 million in assets, $13 million in net loans, $43 million in investments, $41 million in deposits, and $13 million of stockholders' equity at the merger date.

6. Guarantees:

Community does not issue any guarantees that would require liability recognition or disclosure, other than its standby letters of credit. Standby letters of credit written are conditional commitments issued by Community to guarantee the performance of a customer to a third party. Generally, all letters of credit, when issued have expiration dates within one year. The credit risk involved in issuing letters of credit is essentially the same as that which is involved in extending loan facilities to customers. Community generally holds collateral and/or personal guarantees supporting these commitments. Community had issued $87.5 million and $84.2 million of standby letters of credit as of March 31, 2007 and December 31, 2006, respectively. Management believes that the proceeds obtained through a liquidation of collateral and the enforcement of guarantees would be sufficient to cover the potential amount of future payments required under the corresponding letters of credit. The current amount of the liability as of March 31, 2007 and December 31, 2006, for guarantees under standby letters of credit issued is not material.

7. Long-Term Debt:

(in thousands)	**March 31, 2007**	**December 31, 2006**
Outstanding advances from the FHLB of Pittsburgh mature from 2007 to 2017. The advances are collateralized by FHLB stock, certain first mortgage loans and both agency and mortgage-backed securities. The advance rates range from 2.70% to 6.35%, with a weighted average interest rate of 4.58%. Advances totaling $354 million are convertible advances. Convertible advances with an initial fixed-rate period are convertible to variable rate at the option of the FHLB. Convertible advances with an initial variable-rate period at LIBOR-100 basis points are convertible to fixed-rate or to a variable rate tied to a spread over LIBOR. Under the terms of the arrangements, if the FHLB opts to convert advances to variable rate, Community has the ability to prepay the advances at no penalty. At the current time no advances have been converted, and remain at the initial period rate.	**$ 438,196**	$ 315,079

Maturities on long-term debt at March 31, 2007, are as follows for twelve month periods ending as indicated (in thousands):

March 31, 2008	$ 52,439
March 31, 2009	41,822
March 31, 2010	89
March 31, 2011	30,090
March 31, 2012	5,088
Thereafter	308,668
	$ 438,196

8. Stock-Based Plans:

In January, 2007, Community granted 273,000 option awards under its Long-Term Incentive Program. The fair value of the awards was estimated with the following weighted-average assumptions using the Black-Scholes option pricing model:

Dividend yield	3.1%
Volatility	29.2%
Risk-free interest rate	4.5%
Expected life (years)	6.0
Resulting grant-date fair value	$ 6.33

These assumptions are based on multiple factors, including historical exercise patterns of employees in relatively homogeneous groups with respect to exercise and post-vesting employment termination behaviors, expected future exercising patterns for the same homogeneous groups and the historical volatility of Community's stock price.

At March 31, 2007, there was $2.8 million of unrecognized compensation cost related to all share-based payments. This cost is expected to be recognized over a weighted-average period of 4.4 years.

Part 1 - Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

INTRODUCTION

The purpose of this review is to provide additional information necessary to fully understand the consolidated financial condition and results of operations of Community Banks, Inc. ("Community"). Throughout this review, net interest income and the yield on earning assets are stated on a fully taxable-equivalent basis and balances represent average daily balances unless otherwise indicated.

GAAP REPORTING ISSUES

This section of the presentation will summarize the salient GAAP reporting issues associated with presentations of financial information for Community, including: forward-looking statements; critical accounting policies; and GAAP versus "non-GAAP" presentations.

Forward-Looking Statements

Periodically, Community has made, and will continue to make, assertions that may include forward-looking information. Community cautions that forward-looking information disseminated through financial presentations should not be construed as guarantees of future performance. Furthermore, actual results may differ from expectations contained in such forward-looking information as a result of factors that are not predictable. Financial performance can be affected by any number of factors that are not predictable or are out of management's direct control. Examples include: the effect of prevailing economic conditions; unforeseen or dramatic changes in the general interest rate environment; actions or changes in policies of the Federal Reserve Board and other government agencies; the risk associated with global instability; business risk associated with the management of the credit extension function and fiduciary activities. Each of these factors could affect estimates, assumptions, uncertainties and risk used to develop forward-looking information, and could cause actual results to differ materially from management's expectations regarding future performance.

Critical Accounting Policies

The identification of those accounting policies which are deemed to be critical to the application of GAAP on reported results of Community is an important facet of this presentation. Management has identified the applicable promulgations of GAAP that have particular relevance in connection with reported results for the quarter ended March 31, 2007:

- Allowance for Loan Losses: Adequacy of Allowance
- Purchase Accounting for Business Combinations
- "Other than Temporary" Impairment of Investment Securities
- Adoption of Fair Value Accounting

Management believes that the application of its accounting policies and procedures for each of the above items should be considered to be a critical accounting policy to ensure the fair presentation of Community's financial statements.

- *Adequacy of Allowance*

Community applies a systemic methodology in order to estimate the allowance for loan losses. This methodology incorporates management's judgments about the credit quality of the loan portfolio and a disciplined, regimented methodology that is consistently applied. This process requires that a detailed analysis of the loan portfolio be performed on a quarterly basis. This analysis includes a specific individual loan review for any and all loans that meet specific materiality criteria. Such loans are evaluated for impairment under the provisions of Statement of Financial Accounting Standards ("SFAS") No. 114, "Accounting by Creditors for Impairment of a Loan." The portfolio is further stratified to analyze groups of homogeneous loans with similar risk characteristics. Such loans are evaluated under the provisions of SFAS No. 5 "Accounting for Contingencies."

Management considers all known relevant internal and external factors that may affect loan collectibility, as well as particular risks indigenous to specific types of lending. The process is further designed to consolidate the aggregate loss estimates and to ensure that the allowance for loan losses is recorded in accordance with generally accepted accounting principles. The final results are reviewed and approved by executive management. Results are regularly validated by a review of trends associated with loan volume, delinquencies, potential concentrations, or other factors that may influence the methodology used to estimate the allowance for loan losses.

- *Purchase Accounting for Business Combinations*

In June of 2001, the Financial Accounting Standards Board ("FASB") issued SFAS No. 141, "Business Combinations," and SFAS No. 142, "Goodwill and Other Intangible Assets." These standards eliminated the pooling-of-interests method of accounting ("pooling") in favor of purchase accounting. Further, these standards were promulgated to ensure that post-merger financial statements of combined entities are prepared in a manner that best represents the underlying economics of a business combination.

These standards necessitate the application of accounting policies and procedures that entail the use of assumptions, estimates, and judgments that are critical to the presentation of financial information, including the ongoing valuation of intangibles. The ultimate responsibility for the application of these standards and the adequacy of disclosures related thereto rests with management.

- *Other than Temporary Impairment of Investment Securities*

Investment securities are written down to their net realizable value when there is impairment in value that is considered to be other than temporary. The determination of whether or not other than temporary impairment exists is a matter of judgment. Management reviews its investment securities portfolio regularly for possible impairment that is other than temporary by analyzing the facts and circumstances of each investment and the expectations for that investment's performance. As a result of discussions with the SEC regarding the reversal of its application of SFAS No. 159 to certain investment securities, Community recorded an "other than temporary impairment" of $4.4 million as of March 31, 2007. See Note 2 to the consolidated financial statements for a more detailed discussion.

- *Adoption of Fair Value Accounting*

As described in the notes to the consolidated financial statements, Community elected to adopt both SFAS No. 157 "Fair Value Measurements" and SFAS No.159 "The Fair Value Option for Financial Assets and Financial Liabilities" as of January 1, 2007. See Note 2 to the consolidated financial statements for a more detailed discussion.

GAAP versus Non-GAAP

Since 2001, all business combinations must be accounted for under the "purchase accounting" method. Prior to that time, most business combinations in the banking industry had been accounted for under the previously permissible "pooling of interests" method. Like most other financial institutions that have made large acquisitions since the mandate of purchase accounting, Community is now providing certain non-GAAP information to assist investors in their understanding of the effect of acquisition activity on reported results. Many of these disclosures have been designed to overcome comparability issues related to the influence of intangibles (principally goodwill) created in business combinations. Such information is not presented as a substitute for traditional GAAP measurements, but is provided as a supplemental enhancement to improve comparability and investor understanding. Community has augmented its traditional GAAP presentation by providing an extensive reconciliation of relevant GAAP and non-GAAP measures to enhance its disclosures of comparative financial performance.

SUMMARY OF FINANCIAL AND OPERATING RESULTS

Overview

Community Banks, Inc. reported operating results for the first quarter of 2007, including net income of $6.6 million and earnings per share of $0.28. These results included an after tax loss of $2.9 million from the "other than temporary impairment" loss (the "impairment loss") that was recorded for certain investment securities that were sold in early April, 2007. The sale was followed by the reinvestment of sales proceeds, which is expected to increase annualized net interest income by approximately $1.4 million in future periods. See Note 2 to the consolidated financial statements for a more detailed discussion.

Excluding the impact of the $2.9 million after tax impairment loss and other related adjustments, net income and earnings per share reached $9.6 million and $0.41 respectively. These results were 7% below those reported in the first quarter of 2006, but reflected a slight improvement from the results reported in the sequential 2006 fourth quarter. Excluding the impact of the impairment loss, first quarter 2007 performance produced more stabilized funding expenses as compared to the sequential quarter, which contributed to a modest improvement in Community's largest source of revenue, net interest income. Notably, Community reported no loss exposure related to the sub-prime mortgage issues that have adversely influenced first quarter 2007 performance in certain sectors of the financial services industry.

Improvements in core banking industry profit performance have been constrained by the effects of the prevailing interest rate environment. That environment has been distinguished by "inverted yield curve" conditions that have been in place throughout much of 2006 and into early 2007. This yield curve trend has hindered top line revenue growth by narrowing the historical spread between income received from earning assets and the interest paid on deposits and other borrowings. Despite the impact of interest rate trends on both net interest income and profit growth, most other critical performance metrics at Community continued to reflect favorable operating conditions.

Loan and deposit balances reflected quarterly increases from the year ago period, at 5% and 7%, respectively. Net interest margin, a critical determinant of revenue growth for financial institutions, declined from 3.98% to 3.73% between the two periods. At the same time, comparisons of net interest margin to the sequential fourth quarter reflected improvement, as both the yields on earning assets and costs of funding sources moved slightly upward, producing a modest improvement in net interest income. Comparisons to the year ago first quarter reflected the impact of increasing consumer preference for shorter duration time deposits since that time. This increased concentration of higher cost time deposits, combined with only slight improvement in asset yields, resulted in a decline in net interest margin from the year ago period. The lack of improvement in asset yields since the middle of 2006 was attributed to the curtailment of increases in most of the benchmark interest rates that influence asset pricing.

During the first quarter of 2007, Community recorded a provision for loan losses that permitted the allowance for credit losses to keep pace with overall loan growth and sustained the ratio of the allowance to loans at 1.00%. Overall credit quality metrics remained relatively stable with no major changes in Community's asset quality profile since the end of 2006. The provision of $1.3 million was substantially in excess of first quarter net charge-offs of $547,000.

Excluding the impairment loss, non-interest income grew 13% from the first quarter of 2006, a considerable portion of which related to the purchases of an additional insurance agency in May, 2006, and a trust business in September, 2006. Accordingly, the first quarter of 2006 reflected no revenues from these acquired businesses and the increases related thereto produced more than half of the overall increases in total non-interest income. Deposit and service fees continued to experience organic growth, providing most of the remaining improvement in other income.

At the end of 2006, Community announced its intention to accelerate expense saving initiatives related to both the reduction in operating regions from nine to six, and to the introduction of its office rationalization process. In connection with these efforts, Community identified preliminary staffing reductions in the first quarter, the majority of which were facilitated through early retirement, scheduled attrition, or selected staff reductions.

The efficiency ratio, which excludes the effect of the impairment loss, provides a comparison of the relative levels of expenses to revenues.. This ratio declined to 58.3% and reflected improvement from the 61.0% performance in the fourth quarter of 2006. Community continued its emphasis on ensuring that operating expenses are appropriately aligned with its revenue stream. First quarter 2007 expenses grew 7.8% from the first quarter of 2006. The comparative increase from the first quarter of 2006 was largely attributable to the increased expenses associated with the acquired insurance and trust businesses. After excluding these incremental expenses, which were not present in the first quarter of 2006, core expense growth approximated 5%.

Important traditional measures of relative financial performance include return on average assets (ROA) and return on average equity (ROE), which were 0.75% and 5.49%, respectively, for the first three months of 2007. Excluding the impact of the impairment loss and related adjustments, traditional ROE and ROA were 1.10% and 8.04%, respectively. Comparable measures in the first quarter of 2006 were 1.27% and 8.96%.

"Non-GAAP" measures include "return on tangible assets" (ROTA) and "return on tangible equity" (ROTE). These measures include the effect of the impairment loss and related adjustments in the first quarter of 2007 and reached 0.87% and 12.40%, respectively, compared to 1.43% and 20.12% in the first quarter of 2006. The following is a brief summary of these and other non-GAAP metrics that provide a framework for evaluating the comparative performance of Community. "Net operating" or "tangible" results exclude expenses that management considers to be "non-operating." "Net operating" results exclude the after-tax effect of core deposit and other intangible assets amortization and the after-tax effect of merger, conversion and restructuring expenses. Similarly, "tangible" assets and "tangible" equity exclude balance sheet amounts for goodwill, core deposit and other intangible asset balances, net of applicable deferred tax amounts, as appropriate. The following is a comparative presentation of certain critical non-GAAP performance measures for the first quarters of 2007 and 2006. These measures include the effect of the impairment loss and related adjustments on the three months ended March 31, 2007.

	Three Months Ended March 31,	
(Dollars in thousands, except per share data)	**2007**	**2006**
Net operating (tangible) income	$ 7,016	$ 10,994
Average tangible assets	$ 3,285,106	$ 3,124,522
Average tangible equity	$ 229,392	$ 221,552
Operating return on average tangible assets	0.87%	1.43%
Operating return on average tangible equity	12.40%	20.12%
Tangible book value at end of period	$ 9.91	$ 9.19

MERGERS

Immediately after the end of the first quarter, Community completed its mergers with BUCS Financial Corp ("BUCS") and East Prospect State Bank ("East Prospect"). The separate mergers with Owings Mills, Maryland-based BUCS ($145 million in assets) and York County, Pennsylvania-based East Prospect ($57 million in assets) were both completed effective April 1, 2007. These two mergers provide an important market extension into the desirable, adjacent Central Maryland region and bolster Community's position in the vibrant York County, Pennsylvania, market.

On May 1, 2007, Community announced that it had signed a definitive agreement pursuant to which Community will combine with Susquehanna Bancshares, Inc. ("Susquehanna"), under Susquehanna's charter. At the time of the announcement, the value of the transaction was approximately $860 million. Following consummation, the joint franchise will include approximately 240 banking offices in the mid-Atlantic region. The merger is subject to regulatory approval and the separate approvals of the shareholders of both Community and Susquehanna.

BALANCE SHEET

The average balance sheets for the three months ended March 31, 2007 and 2006 were as follows (in thousands):

	March 31,		Change	
	2007	2006	Volume	%
Cash and due from banks	$ 55,542	$ 59,253	$ (3,711)	(6)%
Federal funds sold and interest-bearing deposits	10,701	34,885	(24,184)	(69)%
Investments	682,592	613,891	68,701	11%
Loans	2,404,530	2,289,979	114,551	5%
Allowance for loan losses	(24,022)	(23,172)	(850)	4%
Net loans	2,380,508	2,266,807	113,701	5%
Goodwill and identifiable intangible assets	259,083	258,689	394	---
Other assets	155,763	149,686	6,077	4%
Total assets	$ 3,544,189	$ 3,383,211	$ 160,978	5%
Non-interest bearing deposits	$ 340,580	$ 373,637	$ (33,057)	(9)%
Interest-bearing deposits	2,121,561	1,928,261	193,300	10%
Short-term borrowings	124,985	68,524	56,461	82%
Long-term debt	391,196	467,010	(75,814)	(16)%
Subordinated debt	56,817	44,674	12,143	27%
Other liabilities	22,122	22,598	(476)	(2)%
Total liabilities	3,057,261	2,904,704	152,557	5%
Stockholders' equity	486,928	478,507	8,421	2%
Total liabilities and stockholders' equity	$ 3,544,189	$ 3,383,211	$ 160,978	5%

Changes in Community's statement of condition from the first quarter of 2006 to the first quarter of 2007 reflect the overall economic trends influencing financial institution performance on both a national and regional level. The most pervasive economic trends seem to suggest a higher probability for some softening of economic activity, which is moderating both the growth and profitability of financial institution performance. These trends include a measurable reduction in level of new home construction and home sales, higher energy prices, and a declining level of consumer confidence. Local economic conditions within Community's trading area have remained steady, but are not immune to the more pervasive conditions existing throughout the overall economy.

While conditions on a national level suggest a higher likelihood of an economic slowdown, the actual changes in assets from the year ago period are encouraging. The major category of earning assets, and the most important driver of overall interest income performance, is loan growth. Loan growth, while not robust, did reflect 5% increase from the year ago period. Overall earning assets also grew 5%.

The following table provides a summary of the changes in the various categories of loans (in thousands):

			Change	
	2007	2006	Amount	%
Commercial	$ 895,114	$ 808,108	$ 87,006	11%
Commercial real estate	810,424	799,505	10,919	1%
Residential real estate	151,141	153,282	(2,141)	(1)%
Consumer	547,851	529,084	18,767	4%
Total	$ 2,404,530	$ 2,289,979	$ 114,551	5%

Growth in the first quarter loan balances was fueled primarily by commercial loan growth. Loan growth had been muted in the fourth quarter of 2006 and the improvement in the first three months of 2007 reflected favorable seasonal influences. While commercial loan growth was strong, growth in commercial real estate lending was more subdued. Much of the decline relates to the sequential quarter pay downs of real estate development loans which occurred in the fourth quarter of 2006. Given the perceived softness in the housing industry, a number of commercial borrowers have been reducing their credit facilities and scaling back on development activities until economic conditions exhibit more tangible signs of sustainable improvement.

Deposit balances remain the primary source of core funding and Community recognized growth of 7% from the first quarter of 2006 to the first quarter of 2007, as follows:

			Change	
(in thousands)	**2007**	**2006**	**Amount**	**%**
Demand	$ 340,580	$ 373,637	$ (33,057)	(9)%
Savings & NOW accounts	858,469	826,742	31,727	4%
Time	994,824	900,698	94,126	10%
Time $100,000 or more	268,268	200,821	67,447	34%
	$ 2,462,141	$ 2,301,898	$ 160,243	7%

Comparisons of the various categories of deposit funding sources reflect many of the same trends that were experienced throughout 2006. Rates on time deposits increased throughout 2006, resulting in an overall increase in those categories, partially offset by a reduction in demand deposit balances. The interest rate offerings on short term time deposits were influenced by the steady increase in the benchmark Fed Funds rate through the first six months of 2006. Throughout 2006, the increased rate offerings on short term time deposits, particularly those offerings with maturities under one year, provided sufficient incentive for depositors to commit excess liquidity into higher-yielding, short-term time deposit products. The rates offered on short term time deposits provided both the desired level of liquidity and more competitive pricing for consumers. While demand deposit balances reflected a 9% decline from the year ago period, the levels of demand deposit balances since the middle of 2006 through the first quarter of 2007 have remained relatively stable.

Community also reflected some increases in both wholesale borrowing categories and investment balances. The increases are reflective of ongoing efforts to enhance net interest income growth and asset / liability management during periods characterized by moderate loan growth and subdued economic activity.

RESULTS OF OPERATIONS

Net Interest Income

Community's major source of revenue is derived from intermediation activities and is reported as net interest income. Net interest income is defined as the difference between interest income on earning assets and interest expense on deposits and borrowed funds. Net interest margin is a relative measure of a financial institution's ability to efficiently deliver net interest income from a given level of earning assets. Interest spread, which is the primary component of net interest margin, is the difference between the interest rates received on earning assets and those paid on interest-bearing liabilities. Net interest income, net interest margin, and interest spread are all influenced by the frequency, velocity, and extent of interest rate changes, including the slope of the yield curve, and by the composition and absolute volumes of earning assets and funding sources.

The following table compares net interest income, net interest margin, and interest spread components between the first quarter of 2006 and 2007.

Net Interest Margin – Quarter to Date

(in thousands)	March 31, 2007			March 31, 2006		
	Average Balance	FTE Interest Income/ Expense	Average Rate Earned/ Paid	Average Balance	FTE Interest Income/ Expense	Average Rate Earned/ Paid
Federal funds sold and interest-bearing deposits in banks	$ 10,701	$ 135	5.12%	$ 34,885	$ 393	4.57%
Investments	682,592	10,209	6.07%	613,891	8,901	5.88%
Loans - commercial	895,114	17,792	8.06%	808,108	15,145	7.60%
- commercial real estate	810,424	14,174	7.09%	799,505	13,605	6.90%
- residential real estate	151,141	2,397	6.43%	153,282	2,297	6.08%
- consumer	547,851	9,785	7.24%	528,976	8,526	6.54%
Total earning assets	$3,097,823	$ 54,492	7.13%	$2,938,647	$ 48,867	6.74%
Deposits – savings and NOW accounts	$ 858,469	$ 4,835	2.28%	$ 826,742	$ 3,501	1.72%
- time	1,263,092	14,051	4.51%	1,101,519	9,920	3.65%
Short-term borrowings	124,985	1,564	5.07%	68,524	696	4.12%
Long-term debt	391,196	4,500	4.67%	467,010	5,111	4.44%
Subordinated debt	56,817	1,022	7.29%	44,674	797	7.24%
Total interest-bearing liabilities	$2,694,559	$ 25,972	3.91%	$2,508,469	$ 20,025	3.24%
Interest income to earning assets			7.13%			6.74%
Interest expense to paying liabilities			3.91%			3.24%
Interest spread			3.22%			3.50%
Impact of non-interest funds			0.51%			0.48%
Net interest margin		$ 28,520	3.73%		$ 28,842	3.98%

Changes in net interest income, net interest margin, and interest spread between the two periods were influenced by the same trends experienced in the second half of 2006, as documented in the December 31, 2006, Form 10-K. These trends are apparent from the above comparisons and can be summarized as follows:

- The existence of a generally higher level of short-term interest rates since the first quarter of 2006 and the prolonged presence of an inverted yield curve throughout most of 2006 and into the opening quarter of 2007. Interest rate trends contributed to a 39 basis point increase in earning asset yields between the two periods shown, but were more than offset by a more substantial 67 basis point increase in the cost of interest-bearing liabilities. Consequently, interest spread declined by 28 basis points while net interest margin declined by 25 basis points in the above quarterly comparison.

- A less robust pace of loan growth since mid-year 2006.

- Some favorable influence from enhanced investment yields and higher portfolio balances in the first quarter of 2007.

- A steady increase in short-term interest rate offerings on time deposits that commenced in the first half of 2006, which contributed to the increase in the cost of funds through the end of the first quarter of 2007.

- Ongoing competitive pressure to sustain higher short-term time deposit pricing to maintain and increase funding balances necessary to meet the current level of earning asset growth.

- Consumer preferences for higher-cost rate offerings on time deposits and the increased relative weighting of these deposits as a funding source.

- The Federal Open Market Committee's (FOMC) suspension of further tightening of the benchmark Federal Funds rate since June 30, 2006.

- The pause in the re-pricing of rate sensitive assets since mid-year 2006, while time deposits continued to price upward. The pause was influenced by the suspension of increases in the benchmark rate indices that are the primary influence on the pricing of those assets. At the same time, older, lower-cost time deposits continued to reprice at higher levels.

First quarter comparisons of net interest spread and net interest margin between 2006 and 2007 resulted in declines in both net interest spread, from 3.50% to 3.22%, and in net interest margin, from 3.98% to3.73%. The trends itemized above were the principal catalysts for the decline in these important metrics, and were responsible for the sequential quarterly compression in net interest margin experienced during 2006. Compression during 2006 was illustrated by the decline in net interest margin from 3.98% in the first quarter to 3.71% in the fourth quarter. That decline was characterized by continuous re-pricing of funding sources and a constrained ability to proportionately increase the pricing of rate-sensitive assets. Most of these trends extended into the first quarter of 2007, although further declines in net interest margin were not experienced between the sequential fourth quarter of 2006 and the first quarter of 2007. The first quarter 2007 margin of 3.73% reflected no additional compression as compared to the 3.71% margin recorded in the sequential fourth quarter of 2006. Accordingly, the adverse impact of many of the trends affecting net interest margin results throughout 2006 and into the first quarter of 2007 seemed to abate, or stabilize, by March 31, 2007.

Provision for Loan Losses

During the first quarter of 2007, Community recorded a provision for loan losses that permitted the allowance for credit losses to keep pace with overall loan growth and sustained the ratio of the allowance to loans at 1.00%. Overall credit quality metrics remained relatively stable with no major changes in Community's asset quality profile since the end of 2006. The provision of $1.3 million was substantially in excess of first quarter net charge-offs of $547,000 and higher than the provision of $500,000 recorded in the first quarter of 2006. While most of the underlying credit metrics remained stable, Community did experience an increase in the level of loans included in the non-accrual classification. The increase was attributed to the customary migration of previously-monitored credits and was not deemed to reflect any systemic trend of credit deterioration. A portion of the increase in non-accrual loans related to credits for which Community had recorded partial charge-offs in prior periods. The coverage of the allowance for credit losses to non-accrual loans did decline, however, from 188% at the end of 2006 to 155% at March 31, 2007. Total non-performing assets remained at a comparatively modest 0.65% of outstanding loans at the end of the first quarter.

Non-Interest Income

Non-interest income, excluding investment gains and the impairment loss, increased 17%, to $9.5 million for the quarter ended March 31, 2007, versus $8.1 million in the year ago first quarter. A considerable portion of the 17% increase, nearly half, related to the purchases of an additional insurance agency in May, 2006, and a trust business in October, 2006. The first quarter of 2007 reflected a full three-month period of revenues from these acquisitions, while no comparable revenues were recorded in the first quarter of 2006 due to the timing of the acquisitions. The following summarizes the various components of non-interest income, excluding investment securities gains and other than temporary impairment of investment securities, for the first quarter of both 2007 and 2006:

	Three Months Ended March 31,		
(in thousands)	2007	2006	Increase (Decrease)
Investment management and trust services	$ 1,445	$ 1,013	$ 432
Service charges on deposit accounts	2,996	2,531	465
Other service charges, commissions and fees	2,028	1,700	328
Insurance premium income and commissions	1,176	928	248
Mortgage banking activities	548	468	80
Earnings on investment in life insurance	688	656	32
Other	591	805	(214)
Total non-interest income, excluding investment securities gains and other than temporary impairment	$ 9,472	$ 8,101	$ 1,371

Investment management and trust services income totaled $1.4 million, or more than a 43% increase from the first quarter of 2006. The major component of the increase relates to the fourth quarter 2006 acquisition of a south-central Pennsylvania-based trust business that added approximately $325,000 of quarterly revenues to Community's existing trust business. Total assets under management at March 31, 2007, reached $427 million versus $281 million at the end of the first quarter of 2006. Investment management income also includes the commissions earned from retail investment sales of annuities and other investment products, which has become an increasingly important component of Community's financial services product mix.

Service charges on deposit accounts grew to nearly $3.0 million in the first quarter of 2007, an increase of 18% from the year earlier total of $2.5 million. The most significant portion of this revenue is derived from the OverdraftHonor® program which continues to be made available to an expanding base of customers that meet the prescribed requirements for acceptance into this program.

The remainder of non-interest income, including other service charges and fees, insurance-related revenues, and earnings from life insurance-related investments reflected stable or slightly improved performance. Income from mortgage banking activities continues to be sluggish, owing to reduced refinancing of mortgages and the general decline in housing industry activity. Despite the seasonal decline in mortgage activity that normally occurs in the first quarter of the year, activity in the first quarter of 2007 was modestly ahead of the performance in the first quarter of 2006. Other income was slightly higher than normal, largely from a nonrecurring gain associated with the sale of a discounted loan. Other income in the first quarter of 2006 was similarly inflated due to the prepayment of certain FHLB advances that had been scheduled to re-price at a higher floating rate, precipitating an early retirement and the recognition of a non-recurring gain.

Total non-interest income included $4.4 million of losses related to the impairment loss on certain available-for-sale securities that were subsequently sold in early April, 2007. See Note 2 to the Consolidated Financial Statements for a more complete discussion.

Non-Interest Expenses

Aggregate non-interest expenses grew to $22.1 million, which represented an 8% increase from the first quarter of 2006, when aggregate expenses reached $20.5 million. The following is a quarterly comparison of the expenses within the various components of operating expenses:

	Three Months Ended March 31,		
(in thousands)	2007	2006	Increase (Decrease)
Salaries and employee benefits	$ 12,009	$ 11,418	$ 591
Net occupancy	3,794	3,512	282
Marketing expense	505	575	(70)
Telecommunications expense	525	551	(26)
Amortization of intangibles	661	654	7
Other	4,647	3,823	824
Total non-interest expenses	$ 22,141	$ 20,533	$ 1,608

The efficiency ratio, which compares the relative levels of expenses to revenues, declined to 58.3% and reflected improvement from the 61.0% performance in the sequential fourth quarter of 2006. Community continued its emphasis on ensuring that operating expenses are appropriately aligned with its revenue stream. Ongoing challenges to the revenue stream, caused by the inverted yield curve and less robust loan and asset growth, have intensified management's focus on expense saving opportunities.

While first quarter 2007 expenses grew 7.8% from the first quarter of 2006, expenses exhibited no increase when compared with the more recent fourth quarter. The comparative increase from the first quarter of 2006 was largely attributable to the increased expenses associated with the acquired insurance and trust businesses, a portion of which was concentrated in salary and employee benefits expenses. After excluding these incremental expenses, which were not present in the first quarter of 2006, core expense growth approximated 5%.

At the end of 2006, Community announced its intention to accelerate expense saving initiatives related to both a reduction in operating regions from nine to six, and to the introduction of its more expansive office rationalization process. In connection with these efforts, Community identified initial salary and benefit savings in the first quarter, the majority of which were facilitated through early retirement, scheduled attrition, or selected staff reductions. Community incurred nearly $300,000 of one-time expenses in the opening quarter of 2007, but expects to recognize nearly $1.8 million of related savings on an annualized basis. Additionally, Community is continuing its office rationalization process that has resulted in a more focused review and analysis of under-performing offices and produced strategic delays in previously-planned office openings. These efforts will continue throughout 2007, with additional efficiencies to be realized throughout the remainder of the year.

First quarter expenses normally reflect the impact of annual merit and salary increases, which has a substantial influence over expense comparisons to both the prior year's first quarter and the sequential fourth quarter. In comparing salary and benefits expense from the first quarter of 2007 to the same period in 2006, there was an increase of $591,000, or 5%, which was partially linked to additional expenses from 2006 acquisitions of trust and insurance businesses.

Occupancy expenses grew 8%, from $3.5 million in the first quarter of 2006 to $3.8 million in the same period of 2007. Community continues to experience increases in occupancy expenses related to its legacy office expansion strategy.

Both marketing and telecommunications expenses exhibited slight reductions from the first quarter of 2006 to the first quarter of 2007. Community continues to moderate the growth in discretionary expense categories, consistent with the increased emphasis on expense control.

The other expense category grew from $3.8 million to $4.6 million when comparing the first quarters of 2007 and 2006. Increases were influenced by a number of factors, including a steadily higher level of bank shares tax since the merger of the Blue Ball Bank division in mid-year 2005 and the increased transaction fees associated with higher debit card-based transaction volumes. Community experienced similar, offsetting increases in revenues from these activities during the quarter.

Income Taxes

The reported rate for the first quarter of 2007 was 17%, while the rate for the same period of 2006 was 26%. The reported rate for 2007 was significantly influenced by the impact of the impairment loss on pre-tax income.

CAPITAL

Regulators have established standards for the monitoring and maintenance of appropriate levels of capital for financial institutions. Regulatory capital guidelines are based on a risk-based supervisory approach that has been designed to ensure effective management of capital levels and associated business risk. The following table provides the risk-based capital positions of Community and its banking subsidiary, CommunityBanks, at March 31, 2007, along with a comparison to the various current regulatory capital requirements:

	March 31, 2007	Regulatory Minimum	"Well Capitalized"
Leverage ratio			
Community Banks, Inc.	9.18%	4%	5%
CommunityBanks	8.37%	4%	5%
Tier 1 capital ratio			
Community Banks, Inc.	11.20%	4%	6%
CommunityBanks	10.25%	4%	6%
Total risk-based capital ratio			
Community Banks, Inc.	12.10%	8%	10%
CommunityBanks	11.16%	8%	10%

In early March of 2007, Community executed an issuance of $20 million of fixed-rate subordinated debentures that met the regulatory requirements and associated restrictions for qualification as "Tier 1 capital" and were classified as subordinated debt on the consolidated balance sheet. At the end of the first quarter of 2007, Community had $70 million of subordinated debt that qualified as "Tier 1 capital." The majority of the proceeds of the most recent issuance were utilized to facilitate the cash consideration in the acquisitions of BUCS Financial Corp and East Prospect State Bank on April 1, 2007.

Earnings in the first quarter of 2007 supported a return of capital to shareholders in the form of a cash dividend to shareholders of $0.21 per share.

CONTRACTUAL OBLIGATIONS

Significant contractual obligations at March 31, 2007, are summarized as follows:

	Payments due by period				
(in thousands)	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-term debt	$ 438,196	$ 52,439	$ 41,911	$ 35,178	$ 308,668
Operating lease obligations	39,589	2,210	4,263	4,073	29,043
Subordinated debt	72,167	---	---	---	72,167
Time deposits	1,278,667	926,621	289,074	60,380	2,592
Total	$ 1,828,619	$ 981,270	$ 335,248	$ 99,631	$ 412,470

COMMUNITY BANKS, INC. AND SUBSIDIARIES

PART I - Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations (continued)

Table 1: Reconciliation of GAAP to Non-GAAP Measures: [(1)]

(in thousands)	Three Months Ended March 31, 2007	Three Months Ended March 31, 2006
Income statement data:		
Net income		
Net income	$ 6,587	$ 10,569
Amortization of core deposit and other intangible assets [(1)]	429	425
Net operating (tangible) income	$ 7,016	$ 10,994
Balance sheet data:		
Average assets		
Average assets	$ 3,544,189	$ 3,383,211
Goodwill	(246,400)	(244,775)
Core deposit and other intangible assets	(12,683)	(13,914)
Average tangible assets	$ 3,285,106	$ 3,124,522
Operating return on average tangible assets	0.87%	1.43%
Average equity		
Average equity	$ 486,929	$ 478,507
Goodwill	(246,400)	(244,775)
Core deposit and other intangible assets	(12,683)	(13,914)
Deferred taxes	1,546	1,734
Average tangible equity	$ 229,392	$ 221,552
Operating return on average tangible equity	12.40%	20.12%
At end of quarter:		
Total assets		
Total assets	$ 3,627,739	$ 3,421,562
Goodwill	(246,449)	(244,760)
Core deposit and other intangible assets	(12,363)	(13,599)
Total tangible assets	$ 3,368,927	$ 3,163,203
Total equity		
Total equity	$ 490,564	$ 475,587
Goodwill	(246,449)	(244,760)
Core deposit and other intangible assets	(12,363)	(13,599)
Deferred taxes	1,482	1,854
Total tangible equity	$ 233,234	$ 219,082
Tangible book value at end of period	$ 9.91	$ 9.19

[(1)] Net of related tax effect

PART I - Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk, the exposure to economic loss that arises from changes in the values of certain financial instruments pursuant to factors arising out of the various categories of market risk, can include a number of categories, including interest rate risk, foreign currency risk, exchange rate risk, commodity price risk, etc. For domestic, community-based banks, the vast majority of market risk is related to interest rate risk.

The following table provides a measure of interest rate sensitivity for each category of interest earning assets and interest bearing liabilities at March 31, 2007.

Interest Rate Sensitivity

(in thousands)	1-90 days	90-180 days	180-365 days	1 year or more	Total
Assets					
Federal funds sold	$ 10,199	---	---	---	$ 10,199
Interest-bearing deposits in other banks	32,964	---	---	---	32,964
Investment securities	208,829	20,608	23,595	415,102	668,134
Loans[(1)]	749,291	102,502	190,591	1,399,934	2,442,318
Earning assets	1,001,283	123,110	214,186	1,815,036	3,153,615
Non-earning assets	630	571	1,142	471,781	474,124
Total assets	$ 1,001,913	$ 123,681	$ 215,328	$ 2,286,817	$ 3,627,739
Liabilities					
Savings	$ 241,737	$ 38,419	$ 76,806	$ 525,641	$ 882,603
Time	289,165	170,478	251,062	283,410	994,115
Time in denominations of $100,000 or more	112,924	45,991	57,001	68,636	284,552
Short-term borrowings	67,747	---	---	---	67,747
Long-term debt	12,990	41,952	22,405	360,849	438,196
Subordinated debt	23,196	---	---	48,971	72,167
Interest bearing liabilities	747,759	296,840	407,274	1,287,507	2,739,380
Other liabilities and equity	11,038	11,038	22,075	844,208	888,359
Total liabilities and equity	$ 758,797	$ 307,878	$ 429,349	$ 2,131,715	$ 3,627,739

(1) Includes non-accrual loans.

Interest Sensitivity GAP

(in thousands)	1-90 days	90-180 Days	180-365 days
Periodic	$ 243,116	$ (184,197)	$ (214,021)
Cumulative		58,919	(155,102)
Cumulative GAP as a percentage of total assets	6.7%	1.6%	(4.3)%

The GAP between interest-earning assets and interest-bearing liabilities maturing or repricing within one year was liability sensitive at December 31, 2006 and at March 31, 2007, moving from (9.2)% to (4.3)%.

PART I - Item 4. Controls and Procedures

Under the supervision and with the participation of Community's management, including its Chief Executive Officer and Chief Financial Officer, Community has evaluated the effectiveness of its disclosure controls and procedures as of March 31, 2007. Based upon this evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that Community's disclosure controls and procedures are adequate and effective to ensure that material information relating to Community and its consolidated subsidiaries is made known to them by others within those entities, particularly during the period in which this quarterly report was prepared. There have not been any changes in Community's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the most recent fiscal quarter that have materially affected, or are reasonably likely to materially affect, Community's internal control over financial reporting.

Because of inherent limitations, our disclosure controls and procedures may not prevent or detect misstatements. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

COMMUNITY BANKS, INC. AND SUBSIDIARIES

PART II - OTHER INFORMATION

Item 1 – Legal Proceedings

Various actions and proceedings are presently pending to which Community and/or one or more of its subsidiaries is a party. These actions and proceedings arise out of routine operations and, in management's opinion, will not have a material adverse effect on Community's consolidated financial position or results of operations.

Item 1A – Risk Factors

There have been no material changes from risk factors as previously disclosed in Community's Form 10-K (Item 1A, of Part I) for the year ended December 31, 2006, (filed with the Commission on March 16, 2007).

Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds

Community did not sell any unregistered equity securities during the first quarter of 2007.

In October, 2005, the Board of Directors approved a Stock Repurchase Program under which Community could repurchase up to 787,500 shares of outstanding stock. During the first quarter of 2007, Community purchased 12,300 shares as part of the repurchase program. As of March 31, 2007, 41,600 shares may be purchased pursuant to this program.

In July 2003, Community registered 50,000 shares of its common stock for purchase by employees pursuant to the 401(k) savings plan and the Board of Directors authorized the repurchase of shares of Community common stock to fund the plan. No timetable was set for these repurchases. The table below includes shares repurchased in order to fund the 401(k) plan.

During the first quarter of 2007, no plan or program expired and Community did not determine to terminate any repurchase program.

	Total Number of Shares Purchased	Average Price Paid Per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Capacity to Purchase More Shares Under Repurchase Program
01/1/07-01/31/07	13,069	$24.33	13,069	41,600
02/1/07-02/28/07	4,511	25.69	4,511	41,600
03/1/07-03/31/07	536	24.51	536	41,600

Item 3 – Defaults Upon Senior Securities

Not applicable.

Item 4 – Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5 – Other Information

Not applicable.

PART II - OTHER INFORMATION
(continued)

Item 6 – Exhibits

3.1	Amended and Restated Articles of Incorporation (Incorporated by reference to Appendix A to Community's 2006 Proxy Statement filed with the Commission on March 31, 2006)
3.2	Amended Bylaws (Incorporated by reference to Exhibit 3(ii), attached to Community's Current Report on Form 8-K filed with the Commission on December 14, 2006)
4	Instruments defining the rights of the holders of trust capital securities sold by Community in March, 2007, are not attached, as the amount of such securities is less than 10% of the consolidated assets of Community and its subsidiaries, and the securities have not been registered. Community agrees to provide copies of such instruments to the SEC upon request.
10.1	Form of First Amendment to Stock Option Agreement (Incorporated by reference to Exhibit 10.1 attached to Community's Current Report on Form 8-K filed with the Commission on January 31, 2007)*
31.1	Rule 13a-14(a)/15d-14(a) Certification (Chief Executive Officer)
31.2	Rule 13a-14(a)/15d-14(a) Certification (Chief Financial Officer)
32	Section 1350 Certifications (Chief Executive Officer and Chief Financial Officer)

* Identifies a management contract or compensatory plan or arrangement

SIGNATURES

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

COMMUNITY BANKS, INC.
(Registrant)

Date	June 26, 2007	/s/ Eddie L. Dunklebarger Eddie L. Dunklebarger Chairman and President (Chief Executive Officer)
Date	June 26, 2007	/s/ Donald F. Holt Donald F. Holt Executive Vice President (Chief Financial Officer)

EXHIBIT INDEX

3.1 Amended and Restated Articles of Incorporation (Incorporated by reference to Appendix A to Community's 2006 Proxy Statement filed with the Commission on March 31, 2006)

3.2 Amended Bylaws (Incorporated by reference to Exhibit 3(ii), attached to Community's Current Report on Form 8-K filed with the Commission on December 14, 2006)

4 Instruments defining the rights of the holders of trust capital securities sold by Community in March, 2007, are not attached, as the amount of such securities is less than 10% of the consolidated assets of Community and its subsidiaries, and the securities have not been registered. Community agrees to provide copies of such instruments to the SEC upon request.

10.1 Form of First Amendment to Stock Option Agreement (Incorporated by reference to Exhibit 10.1 attached to Community's Current Report on Form 8-K filed with the Commission on January 31, 2007)*

31.1 Rule 13a-14(a)/15d-14(a) Certification (Chief Executive Officer)

31.2 Rule 13a-14(a)/15d-14(a) Certification (Chief Financial Officer)

32 Section 1350 Certifications (Chief Executive Officer and Chief Financial Officer)

* Identifies a management contract or compensatory plan or arrangement