

UNITED STATES BANKRUPTCY COURT
DISTRICT OF MAINE

_____))	
In re:))	Chapter 11
PEGASUS SATELLITE TELEVISION, INC., et al.,))	Case No. 04-20878
Debtors.))	Joint Administration Requested
_____))	

**MOTION OF THE DEBTORS AND DEBTORS IN
POSSESSION FOR AN ORDER AUTHORIZING, BUT NOT REQUIRING,
THE DEBTORS TO (I) HONOR CERTAIN PREPETITION OBLIGATIONS
TO CUSTOMERS, AND (II) CONTINUE THEIR PREPETITION
CUSTOMER POLICIES AND PROMOTIONAL PROGRAMS**

Pegasus Satellite Television, Inc. and certain of its subsidiaries and affiliates, each a debtor and debtor-in-possession herein (collectively, the “Debtors”),¹ hereby submit this motion (the “Motion”) for an order pursuant to sections 105(a) and 507(a)(6) of title 11 of the United States Code (the “Bankruptcy Code”) authorizing, but not requiring, the Debtors to honor certain prepetition obligations to customers and to continue customer accommodation programs and practices, as more fully described herein, in the ordinary course of business (such prepetition customer obligations, accommodation programs and practices together, the “Customer Practices”). The facts and circumstances supporting this Motion are set forth in the concurrently filed Affidavit of Ted S. Lodge, President, Chief Operating Officer and Counsel of Pegasus

¹ The Debtors are: Argos Support Services Company, Bride Communications, Inc., B.T. Satellite, Inc., Carr Rural TV, Inc., DBS Tele-Venture, Inc., Digital Television Services of Indiana, LLC, DTS Management, LLC, Golden Sky DBS, Inc., Golden Sky Holdings, Inc., Golden Sky Systems, Inc., Henry County MRTV, Inc., HMW, Inc., Pegasus Broadcast Associates, L.P., Pegasus Broadcast Television, Inc., Pegasus Broadcast Towers, Inc., Pegasus Media & Communications, Inc., Pegasus Satellite Communications, Inc., Pegasus Satellite Television of Illinois, Inc., Pegasus Satellite Television, Inc., Portland Broadcasting, Inc., Primewatch, Inc., PST Holdings, Inc., South Plains DBS, LP., Telecast of Florida, Inc., WDSI License Corp., WILF, Inc., WOLF License Corp., WTLH License Corp.

Satellite Communications, Inc., in Support of First Day Motions (the "Lodge Affidavit"). In addition, the Debtors respectfully state as follows:

STATUS OF THE CASE AND JURISDICTION

1. On June 2, 2004 (the "Petition Date"), each of the Debtors filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code, and motions or applications seeking certain typical "first day" orders, including an order to have these cases jointly administered.

2. The Debtors have continued in possession of their respective properties and have continued to operate their businesses as debtors in possession pursuant to sections 1107(a) and 1108 of the Bankruptcy Code.

3. No request has been made for the appointment of a trustee or examiner and no official committee has yet been established in these cases.

4. The Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C. § 157(b)(2). Venue is proper in this Court pursuant to 28 U.S.C. §§ 1408 and 1409. The statutory predicates for the relief sought herein are 11 U.S.C. §§ 105(a) and 507(a)(6).

BACKGROUND FOR THE MOTION

5. Pegasus Satellite Television, Inc. ("PST"), together with its subsidiaries, is the nation's largest independent provider of DIRECTV® programming. Organized in 1996 as a Delaware Corporation, PST is headquartered in Marlborough, Massachusetts. PST is a wholly owned indirect subsidiary of Pegasus Satellite Communications, Inc.

6. The Debtors' principal operating business is its direct broadcast satellite ("DBS") business.² Specifically, the Debtors provide DIRECTV programming services to rural households across the United States and, as of December 31, 2003, had in excess of 1.1 million subscribers and the exclusive right to distribute DIRECTV services to approximately 8.4 million rural households in certain territories within 41 states.

7. DBS services are digital broadcasting services that require a subscriber to install or have installed a satellite receiving antenna (or dish) and a digital receiver. DIRECTV, in particular, requires subscribers to have a satellite dish, which can be as small as 18 inches in diameter depending on the services received, to which DIRECTV directly transmits programming services via five high power Ku band satellites. The Debtors in turn offer certain core programming packages to subscribers, which vary according to channels delivered and price.

8. The Debtors maintain an independent retail network through dealer relationships to distribute DIRECTV programming. The Debtors have expanded this network to include over 4,000 consumer electronics stores and other independent retailers serving rural areas in the Debtors' service area. Today, the Debtors' retail network is one of the few sales and distribution channels available to digital satellite service providers seeking broad and effective distribution in rural areas throughout the continental United States.

9. As of March 31, 2004, the Debtors had assets aggregating approximately \$1.6 billion related to their DBS business, which generated net revenues of approximately \$831.2 million during calendar year 2003. The Debtors employ approximately 943 employees.

² Debtor Pegasus Media & Communications, Inc. also conducts television broadcast operations through twelve (12) subsidiaries, all of which have filed voluntary petitions under chapter 11 and are Debtors in these cases.

Satellite Programming Services

10. The Debtors generally offer two options for acquiring the equipment necessary to receive DIRECTV programming: the Pegasus Digital One Plan and the Standard Sale Plan. Under the Pegasus Digital One Plan, subscribers³ are provided with equipment, consisting of a satellite receiving antenna (dish) and one or more set top receivers, obtain DIRECTV programming for a monthly programming fee, enter into an initial 12 month commitment secured by a credit card, and enjoy the benefits of repair service without additional monthly cost (subject to certain limitations). Under this plan, the Debtors retain title to the set top receivers and remote controls provided to subscribers. Subscribers who terminate service but do not return equipment and access cards are assessed equipment nonreturn fees and may be assessed access card nonreturn fees. Failure to satisfy the 12 month commitment, including, in some instances, downgrading of service, typically results in the imposition of cancellation fees.

11. Under the Standard Sale Plan, subscribers obtain equipment consisting of a satellite receiving antenna (dish) and one or more set top receivers and obtain DIRECTV programming for a monthly programming fee. Unlike the Pegasus Digital One Plan, the subscribers own the equipment under the Standard Sale Plan. The Debtors require most Standard Sale Plan subscribers to make an initial 12 month commitment. Failure to satisfy the 12 month programming commitment by those subscribers required to make the commitment typically results in the imposition of cancellation fees. The imposition of cancellation fees is intended to reimburse the Debtors in part for their costs of special introductory promotional offers, equipment and installation subsidies paid to retailers in order to induce those retailers to provide these items at a low cost or no cost to subscribers, and dealer commissions.

³ This Motion shall use the term “customer” and “subscriber” interchangeably.

12. Prior to the Petition Date and in the ordinary course of their businesses, the Debtors engaged in certain practices to develop and sustain a competitive position in the marketplace for their products and services. Among these practices have been warranties, rebates, alleged defective product return policies, and other similar programs, practices and commitments directed at customers. Several of these Customer Practices are described in greater detail below. The common goals of the Customer Practices have been to meet competitive pressures, ensure customer satisfaction, and generate goodwill for the Debtors – thereby retaining current customers, attracting new ones, and ultimately enhancing net revenue.

RELIEF REQUESTED

13. By this Motion, the Debtors respectfully request an order authorizing, but not requiring, the Debtors, in their business judgment, to (i) perform such of their prepetition obligations related to the Customer Practices as they see fit, and (ii) continue, renew, replace, implement new, and/or terminate such of the Customer Practices as they see fit, in the ordinary course of business, without further application to the Court. Accordingly, the Debtors desire to continue during the postpetition period those Customer Practices that they believe were beneficial to their businesses and cost-effective during the prepetition period. The Debtors believe that such relief is necessary to preserve, during the postpetition period, their critical business relationships with their 1.1 million customers and goodwill for the benefit of the estates.

14. In light of the fact that some of the Customer Practices, as they relate to prepetition agreements regarding the Debtors' products and services, may represent unperformed prepetition obligations of the Debtors and may evidence prepetition claims against the Debtors, the Debtors seek this Court's authorization to perform its obligations related to Customer Practices.

15. The Debtors estimate that the aggregate cost of performing their prepetition obligations in regard to the Customer Practices will be approximately \$1,241,027, with the exception of those services for which customers have prepaid prior to the Petition Date. Most, if not all, of the estimated costs detailed herein will be incurred by the Debtors in the form of replacement products and credit obligations. Accordingly, the Debtors submit that the cash outlay required to continue the Customer Practices postpetition is extremely modest given the scope of these cases.

16. The following are general descriptions of the prepetition customer obligations relating to the Debtors' Customer Practices:

Description of Customer Practices and Related Prepetition Obligations

A. Customer Pre-Payment

17. The Debtors bill subscribers in advance of their monthly services. As a result, subscribers must pre-pay for programming services each month. In addition, certain of the Debtors' customers may pay for programming services up to one year in advance. The only programming that the Debtors do not charge for in advance are pay-per-view movies and events. Accordingly, as of the Petition Date, the Debtors owe programming services to almost all of their customers with respect to customer payments made prior to the Petition Date. Through this Motion, the Debtors request authority from the Court to continue providing DIRECTV programming services in the ordinary course of the Debtors' business and honor their obligations to subscribers who have prepaid for programming services.

18. In addition to the pre-payment of programming services, the Debtors may also have obligations relating to installation services or equipment that their customers purchased

via credit card payment prior to the Petition Date. In general, when a subscriber makes a credit card purchase of equipment or installation services, there may be a few days of separation between the date the Debtors charge the subscriber's credit card and the rendering of the installation services or the actual delivery of the equipment. As a result, the Debtors request authority from the Court to continue operating in the ordinary course of business and fulfill these obligations to their customers during the post-petition period that may have been purchased prior to the Petition Date.

B. Customer Rebate Program

19. The Debtors offer rebates to certain of their new customers that currently range between \$50 and \$100 depending on the respective customer's credit score, the type of offer and the selected programming packages. The rebates are paid in the form of programming credits that are applied to the customer's account. The rebates are generally credited to the customer's account within four to eight weeks, or over a series of months, after receipt of the customer's rebate application or upon activation in some cases. In the event the customer terminates its programming prior to the exhaustion of the rebate, the remaining credit is deemed forfeited and will not be applied against any early termination fees or other fees and charges that accrue on the customer's account.

20. The rebates are offered to certain prospective customers to incentivize such customers to subscribe to the Pegasus Digital One Plan. The Debtors' failure to honor the rebates payable to its customers would significantly erode the Debtors' new customer base and impair the Debtors' ability to successfully attract additional subscribers. In the event that the Debtors did not honor such rebate claims, those customers with rebate claims may attempt to

offset those claims against the amount they owe the Debtors. As such, payment of the rebate claims may have minimal impact on the funds available to the Debtors' unsecured creditors.

21. As of the Petition Date, the Debtors estimate a liability of \$125,712 for the cost of rebates arising from prepetition agreements with certain subscribers. However, in light of the fact that these rebates are granted in the form of a credit applied to a particular customer's account, the Debtors do not believe they have any cash liability to their customers with respect to the rebate claims.

C. Warranty and Alleged Defective Return Policies

22. Pursuant to the Pegasus Digital One Plan, the Debtors lease equipment to subscribers of DIRECTV programming services and offer warranties relating to certain components of the leased equipment. In particular, the warranties cover the repair or replacement of any inoperable portion of covered leased equipment that has been used properly in accordance with its intended purpose and instructions.

23. Upon a customer request for repair or replacement, the Debtors determine the appropriate method of servicing the inoperable equipment, which decision is in their sole discretion. The Debtors contract with third parties to perform all repair work covered by the warranties. Although the Debtors do not believe that as of the Petition Date they have any cash liability on account of these warranty claims, the Debtors respectfully request that the Court authorize them to continue performing their warranty obligations in the ordinary course of business after the Petition Date.

24. In addition, for those customers who choose to purchase rather than lease equipment, the Debtors offer in the ordinary course of their business a service plan, which

provides customers an extended warranty on their equipment. In order to purchase the service plan, customers pay a month-to-month fee that covers certain repairs or the replacement of defective equipment. As with the warranty for leased equipment, the Debtors contract with a third party provider to perform all repair work covered by the service plan. The Debtors, through a third party provider, have an insurance policy in force that guarantees the performance of PST's obligations under the service plan. In the event the Debtors fail to pay any valid claim under the service plans within sixty days after proof of loss has been filed, or fail, in the event of cancellation, to refund the unearned portion of the service plan contract price, the customer is entitled to make a direct claim against the insurer. Although the Debtors do not believe that as of the Petition Date they have any cash liability on account of the service plans, by this Motion, the Debtors request this Court's authority to continue performing their obligations pursuant to those service plans purchased prepetition by certain of their programming customers.

D. Customer Deposit Obligations

25. In the ordinary course of the Debtors' business, the Debtors require a small segment of their customers to remit cash deposits in exchange for the use of an "access card" in certain circumstances. The access card provides security and encryption information and allows subscribers to control the use of their programming systems. The access card also allow the Debtors to capture billing information that is specific to each customer's account. Although most new subscribers obtain an access card when they purchase new equipment, in certain instances subscribers may require replacement access cards when they purchase used equipment or have a lost, stolen or damaged access card, for example. In order to receive a replacement access card, subscribers must deposit \$90 with the Debtors, which is charged to the particular subscriber's DIRECTV programming account. Subscribers are eligible to receive a

refund of this \$90 deposit only upon the return of an undamaged original card within 10 days of the receipt of the replacement card. In addition, if the subscriber returns a different access card or a card that cannot be linked to the original access card, the subscriber is refunded only \$40 of the deposit. After the return of the card, the Debtors refund the deposit by issuing a credit to the subscriber's DIRECTV programming account.

26. The Debtors possess a number of customer deposits that were deposited prior to the Petition Date. It is unclear whether portions of the customer deposits relate to the prepetition period, because the use of the access cards by the Debtors' customers straddles the prepetition and post-petition periods. Thus, out of an abundance of caution, the Debtors seek authority to refund certain customer deposits pursuant to the access card deposit program, including those deposits that may relate to the prepetition period, as and when required in the ordinary course of business. The Debtors believe that they may be required to refund an aggregate amount of customer deposits held as of the Petition Date of approximately \$193,650.

E. General Customer Refunds

27. In the ordinary course of the Debtors' business, the Debtors have maintained certain refund policies under certain reasonable circumstances designed to accommodate their customers' needs. These general customer refunds relate to certain issues that arise in the course of providing DIRECTV programming services or related equipment and include, without limitation, billing or programming errors, problems with programming service, problems with equipment, termination of service where programming was prepaid and other similar refunds and credits.

28. The Debtors hereby seek authority to honor their general customer refund obligations in accordance with their prepetition policies and practices. The Debtors believe that the aggregate amount of General Customer Refunds that have accrued and that are projected to accrue in respect of prepetition customer obligations prior to the Petition Date is approximately \$53,207.

F. Special Promotional Programs

29. From time to time in the ordinary course of their business the Debtors make special promotional offers. Among other things, these programs may be used to encourage customers to sign up for special programming channels or to utilize pay-per-view programming options. Such offers may be in the form of credits to the subscriber's account or coupons that may be exchanged for an account credit. The Debtors estimate that as of the Petition Date an aggregate potential liability of approximately \$868,458 on account of special promotional programs. However, of this aggregate total, \$456,8080 relates to coupons for pay-per-view events. Historically, only approximately 10% of such coupons are actually redeemed by the Debtors' subscribers. As a result, the Debtors believe that their actual liability with respect to special promotional programs could be significantly lower than that estimated herein.

APPLICABLE AUTHORITY

30. The Debtors seek authorization pursuant to section 105(a) and 507(a)(6) of the Bankruptcy Code to continue the Customer Practices and to perform certain prepetition obligations in respect thereof as necessary. Numerous courts have used their section 105(a) equitable powers under the necessity of payment doctrine⁴ to authorize payment of a debtor's prepetition obligations where, as here, such payment is necessary to effectuate the "paramount

⁴ This doctrine, first articulated by the United States Supreme Court in Miltenberger v. C. & S.W.R. Co., 106 U.S.

purpose” of chapter 11 reorganization, which is to prevent the debtor from going into liquidation and preserve the debtor’s potential for rehabilitation. See In re Boston & Maine Corp., 634 F.2d 1359, 1382 (1st Cir. 1980), cert. denied sub nom. Meserve v. Chesapeake & O.R. Co., 101 S.Ct. 1518 (1981) (recognizing, in the railroad reorganization context, the existence of judicial authority to authorize trustees in reorganization cases to pay claims where such payment is necessary for the railroad’s continued ability to operate and reorganize); In re Lehigh & New England Ry., 657 F.2d 570, 581 (3d Cir. 1981) (holding that “if payment of a claim which arose prior to reorganization is essential to the continued operation of the [business] during reorganization, payment may be authorized even if it is made out of the corpus”); In re Ionosphere Clubs, Inc., 98 B.R. 174,176-77 (Bankr. S.D.N.Y. 1989) (citing NLRB v. Bildisco & Bildisco, 465 U.S. 513, 528 (1984)) (doctrine “recognizes the existence of the judicial power to authorize a debtor in a reorganization case to pay pre-petition claims where such payment is essential to the continued operation of the debtor”); see also In re James A. Phillips, Inc., 29 B.R. 391, 394-95 (S.D.N.Y. 1983) (upholding the bankruptcy court’s order authorizing the debtor to make postpetition payment of prepetition claims in the ordinary course without notice and a hearing). Ultimately, the “necessity of payment” doctrine is intended to facilitate the paramount goal of chapter 11; namely, “facilitating the continued operation and rehabilitation of the debtor...” Ionosphere Clubs, 98 B.R. at 176.⁵

31. The loyalty and continued patronage of the Debtors’ customers is critical to the Debtors’ financial health and reorganization prospects. Where retaining loyalty and

286, 311-12 (1882), recognizes the existence of judicial power to authorize a debtor in a reorganization case to pay prepetition claims where such payment is essential to the continued operation of the debtor.

⁵ Although some courts in other jurisdictions have declined to allow the payment of a prepetition debt prior to plan confirmation in certain circumstances, the rationales employed by those courts do not bar payment of the prepetition obligations to the customers in the instant case where significant value is derived from making such payments and

patronage of customers is critical to a successful reorganization, numerous courts, including courts in this Circuit and elsewhere, have granted relief similar to that requested herein. See, e.g., In re UAL Corporation, et al., Case No. 02-48191 (ERW) (Bankr. N.D. Ill. Dec. 11, 2002) (authorizing continuation of numerous customer programs including frequent flier programs and granting authority to honor ticket holder claims); In re Budget Group, Inc., et al., Case No. 02-12152 (MFW) (Bankr. D. Del. 2002) (authorizing debtors to, among other things, honor customer deposit obligations and pay customer refund, reimbursement and supplemental insurance obligations); In re US Airways Group, Inc., et al., Case No. 02-83984 (SSM) (Bankr. E.D. Va. Aug. 12, 2002) (authorizing continuation of numerous customer programs including frequent flier programs and granting authority to honor ticket holder claims); In re WorldCom, Inc., et al., Case No. 02-13533 (AJG) (Bankr. S.D.N.Y. July 23, 2002) (authorizing continuation of numerous customer service programs including promotional services, billing credits, returns and exchanges and allowing debtors to honor customer deposits); ANC Rental Corporation, et al., Case No. 01-11200 (MFW) (Bankr. D. Del. Dec. 17, 2001) (authorizing payment of customer and consumer obligations); In re NationsRent, Inc., Case No. 01-11628 (PJW) (Bankr. D. Del. Dec. 18, 2001) (authorizing payment of customer obligations in the ordinary course of business, including rebates, credits, re-rent charges, deposit refunds and special order charges); Trans World Airlines, Inc., et al., Case No. 01-0056 (SLR) (Bankr. D. Del. Jan. 10, 2001) (authorizing debtors to continue using customer programs and practices in the ordinary course of business); In re Trend Lines, Inc., Case No. 00-15431 (CJK) (Bankr. D. Mass. Aug. 17, 2000) (authorizing debtor to honor gift certificates and store credits); In re United Artists Theatre Company, et al., Case No. 00-3519 (SLR) (Bankr. D. Del. Sept. 5, 2000) (authorizing debtors to continue

the customer payments would otherwise receive priority treatment under section 507(a)(6). See In re Kmart Corp., 359 F.3d 866 (7th Cir. 2004).

customer programs and practices); In re Filene's Basement, Inc., Case No. 99-16984 (Bankr. D. Mass. Aug. 24, 1999) (authorizing continuation and payment of certain prepetition consumer practices).

32. The Debtors believe that most, if not all, of their prepetition obligations relating to Customer Practices are owed to individual consumers. As a result, the Debtors believe that up to \$2,225 per individual of most of these obligations are entitled to priority in payment under section 507(a)(6) of the Bankruptcy Code.⁶ Because such claims are entitled to priority in payment under section 507(a)(6), such claims would have to be paid in full under any plan of reorganization. 11 U.S.C. § 1129(a)(9). Furthermore, the Debtors believe that it is important to honor the prepetition customer obligations in order to maintain good customer relations.

33. The success, viability and revitalization of the Debtors' business are dependent upon the development and maintenance of customer loyalty. The commencement of the Debtors' chapter 11 cases will no doubt create apprehension on the part of the 1.1 million customers or potential customers regarding their willingness to commence or continue doing business with the Debtors. The Debtors believe that without the requested relief, the stability of the Debtors' business will be significantly undermined, and otherwise loyal customers may explore alternative pay television options. The damage that would result if the Debtors failed to honor their prepetition obligations with respect to Customer Practices significantly outweighs any detriment to the Debtors' creditors or their estates. To preserve the value of their businesses, the Debtors must be permitted, in their sole discretion, to continue honoring or paying all Customer Practices without interruption or modification. In addition, to provide necessary

⁶ The Debtors believe that it is highly unlikely that any individual customer could have more than \$2,225 of such

assurances to customers on a going-forward basis, the Debtors request authority to continue honoring or paying all obligations to customers that arise from and after the Petition Date in the ordinary course of the Debtors' business.

34. Accordingly, authorizing the Debtors to honor their prepetition obligations to customers and to continue their Customer Practices is in the best interests of the Debtors, their estates, and their creditors.

NOTICE

35. Notice of this Motion has been given to (i) the United States Trustee for the District of Maine; (ii) the Debtors' fifty (50) largest unsecured creditors on a consolidated basis, as identified in their chapter 11 petitions; (iii) the administrative agents for the credit facilities of Pegasus Media & Communications, Inc. and Pegasus Satellite Communications, Inc. ("PSC") and (iv) each of the indenture trustees for each series of notes of PSC. The Debtors submit that in light of the nature of the relief requested, no further notice is required.

NO PRIOR REQUEST

36. No prior request for the relief sought in this Motion has been made to this or any other Court.

obligations outstanding.

WHEREFORE, the Debtors respectfully request the Court enter an order, substantially in the form attached hereto, authorizing, but not directing, the Debtors to (i) honor certain prepetition obligations to customers as described more fully herein, (ii) continue the Customer Practices in the ordinary course of business, and (iii) granting such other and further relief as the Court deems just and proper.

Dated: Portland, Maine
June 2, 2004

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