

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 FOR ORDER PURSUANT TO 11 U.S.C. §§ 363(b) AND 363(c)(1)
AUTHORIZING, BUT NOT REQUIRING, DEBTORS TO CONTINUE TO
OPERATE IN THE ORDINARY COURSE, INCLUDING PAYMENT OF PRE-
PETITION DATE CLAIMS, WITH RESPECT TO NON-DEBTOR DEALERS**

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 (“Motion”) requesting entry of an order pursuant to sections 363(b), 363(c)(1) and 105(a) of title 11 of the United States Code (the “Bankruptcy Code”) authorizing, but not requiring, the Debtors to continue to operate in the ordinary course of business and maintain their business relationships with respect to the Debtors’ non-debtor dealers, including payment of certain pre-Petition Date amounts owed to the dealers. 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 Satellite Communications, Inc., in Support of First Day Motions (the “Lodge Affidavit”). In further support of the Motion, the Debtors respectfully state as

follows:

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.

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 and legal predicates for the relief sought herein are sections 363(b), 363(c)(1) and 105(a) of the Bankruptcy Code.

BACKGROUND OF THE DEBTORS

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.

Dealers

10. The Debtors obtain new subscribers for their DIRECTV programming services through several channels of distribution. The most significant method of distribution is the Debtors' independent retail network, which consists of dealer relationships with over 4,000 dealers (the "Dealers"), as discussed above. These Dealers are not employees of the Debtors. In order to become a retail Dealer for the Debtors, a prospective Dealer must enter into a Retail Dealer Agreement, which provides certain valuable protections to the Debtors and may be terminated for any reason or no reason upon written notice by either the Dealer or PST. The Debtors' primary commission plan with the Dealers involves the marketing of the Pegasus Digital One Plan (the "Digital One Plan").³ This commission plan is generally governed by the Dealer Rules, Policies, and Procedures, restated as of May 10, 2004 (the "Dealer Rules"). In general, the Dealer Rules provide that the Dealers will market the Pegasus Digital One Plan (the "Program") to residential subscribers who are not current DIRECTV programming subscribers and who have not subscribed to DIRECTV programming through the Debtors during the prior twelve months. The Dealers are responsible for enrolling subscribers to the Debtors' DIRECTV programming, providing subscribers with the necessary equipment, and arranging for installation of the equipment.

11. The Dealers are typically paid directly through a variety of incentive programs, including equipment subsidies, installation subsidies, commissions, and/or flex payments. The Debtors change these incentives from time to time in accordance with certain business initiatives to encourage and reward particular Dealer behavior or to achieve a particular mix of sales offers. In addition, the Dealers may participate in the Pegasus Cooperative

Advertising Program (the “Cooperative Advertising Program”). Under the Cooperative Advertising Program, eligible Dealers are allocated monthly cooperative advertising funds to offset a certain percentage of their qualified advertising expenditures.

12. The strength of the Debtors’ DBS business is based on the Debtors’ widespread national presence in rural markets. In contrast to metropolitan areas, it is difficult to establish sales and distribution channels in rural areas. Most retailers in rural areas are independently owned and operate a limited number of store locations that serve large geographic areas. As a result, the Debtors rely on their 4,000 independent Dealers to distribute DIRECTV programming services to certain areas of the country that are otherwise difficult to penetrate. The Debtors’ ability to maintain a network of Dealers and to penetrate rural markets on a wide-scale basis is critical to the Debtors’ success in its restructuring efforts. Furthermore, the Debtors’ operations are dependent upon obtaining a sufficient number of quality subscribers and retention of subscribers for extended periods of time. The Debtors’ Dealer compensation and incentive programs are designed to ensure that the Dealers maximize their efforts in enlisting new and maintaining existing quality subscribers to the Debtors’ DIRECTV programming services.

RELIEF REQUESTED

13. By this Motion, the Debtors request the entry of an order granting the Debtors authority, in their discretion, to operate in the ordinary course of business and to maintain their business relationships with the Dealers including the performance or payment of certain pre-Petition Date obligations the Debtors owe to their Dealers. The Debtors believe it is

³ In addition to the Pegasus Digital One Plan, the Dealers may also market the Pegasus Standard Sale Plan (the “Standard Sale Plan”). The Standard Sale Plan contains the same general commission programs as the Digital

likely that they will assume their Dealer agreements during the course of the reorganization and therefore any prepetition amounts owed to the Dealers would likely be considered cure obligations at the time of assumption.

14. The Debtors believe the relief requested herein is necessary to their reorganization, because the Dealers are essential to the Debtors' overall business and the Debtors believe that a failure to pay the prepetition amounts owing to the Dealers will have a material, adverse effect on the Debtors' business. First, the Dealers sole source of revenue from the sale of DBS programming and equipment for the Debtors is from the commission programs; the Dealers do not receive any profit margin on the satellite equipment they sell. In addition, although the Dealers must comply with certain performance standards under their contracts with PST, the agreements do not obligate the Dealers to sell a pre-defined number of programming packages or to aggressively solicit new customers. In other words, the Dealers' incentive to expend the effort to sell the Debtors' DBS services is tied directly to the Dealers' commission package not to any express covenants or other agreements in the Dealer Retail Agreement. Accordingly, the Debtors believe that if the Dealers are not paid on account of the prepetition obligations, the Dealers can and will discontinue or substantially reduce their sales efforts on behalf of the Debtors, thereby impeding the Debtors' access to quality, credit-worthy subscribers in rural markets. Furthermore, many of the Dealers also provide services to the Debtors' existing subscribers. If the Dealers discontinue their sales operations on account of non-payment by the Debtors, they may also discontinue servicing the Debtors' current subscribers, which may cause defections of the Debtors' existing customers.

15. Second, the uninterrupted payment of the Dealers is critical to maintaining the Dealers' allegiance to the Debtors.⁴ One factor contributing to the Dealers' loyalty to the Debtors during the prepetition period was the Debtors' ability to make timely payments to the Dealers. Many of the Dealers are dual providers of the DBS services offered by the Debtors and the satellite broadcast programming services offered by the Debtors' competitors. In many of the Debtors' sales territories, the various satellite service providers compete intensely for market share by offering generous compensation packages to Dealers and competitive programming packages to customers. In the event the Dealers go unpaid, the Debtors believe that the Dealers may channel their efforts to market the products and services of the Debtors' competitors against the Debtors' DBS services, or they may violate their obligations under the to the Debtors under the Retail Dealer Agreement by soliciting the Debtors' existing customers (with whom they have pre-existing relationships) to transfer their programming to one of the Debtors' competitors.

16. The Debtors' concerns over Dealer and customer defections are particularly acute because the industry has seen significant disruption and volatility in the past. In 2002, Echostar, one of the Debtors' competitors, made an attempt to acquire DIRECTV. Although this acquisition was ultimately unsuccessful, it caused the Dealers to question the Debtors' future in the DBS industry, despite the Debtors' clear communication to its Dealers that such an acquisition would leave the Debtors' unaffected. Similarly, the media attention surrounding the on-going litigation between the Debtors and DIRECTV has raised doubts among the Dealer network regarding the Debtors' position in the DBS business and prompted inquiries regarding the litigation's impact on the Debtors or the effect it will have on the individual

⁴ Furthermore, because of the small size of certain of the Dealers, any disruption in the payments to the Dealers could have an adverse effect on their operations. Many of the Dealers are small, independently run operations that are dependent on receiving timely payment from the Debtors for their livelihood and may suffer hardship if not paid. If these locations are forced to close their doors, the Debtors may not have any presence in

Dealers. Based on the recent past, the Debtors believe that the filing of these chapter 11 cases will add to the Dealers' uncertainty concerning the Debtors' future. The Debtors believe that paying the Dealers on account of the prepetition obligations will reassure the Dealers that the Debtors intend to, and will in fact, continue performing their obligations to the Dealers during the postpetition period.

17. On account of these factors, if certain Dealer locations refused to deal with the Debtors or were forced to cease operations, the effect of this failure to serve the Debtors' 1.1 million customers in these territories would be very damaging to the Debtors' business and their ability to complete a successful chapter 11 process. The Debtors' goodwill, national presence, and brand recognition, which are enhanced by these locations, would be substantially harmed by a loss of locations and the resulting erosion of the Debtors' customer base, geographic service area and revenue streams. The Debtors' ongoing business efforts require them to fully serve customers in their exclusive territories, which requires the full support of the entire Dealer network.

18. The Debtors compensate their Dealers weekly in arrears by a lump sum payment to each Dealer for each of the Dealer programs. Dealer compensation includes a mix of commission programs, equipment and installation subsidies, bonus programs and cooperative advertising programs. As of the Petition Date, the Debtors' estimate the aggregate cost of performing all of their prepetition obligations owed to their Dealers will be approximately \$1,224,524.

these locations.

APPLICABLE LAW

19. The Court has the authority to permit the Debtors to pay pre-petition amounts owing to the Dealers pursuant to sections 363(b) and 105(a) of the Bankruptcy Code. The fundamental purpose of a chapter 11 reorganization is to rehabilitate the debtor's business to preserve jobs and maximize value for creditors and shareholders. To help accomplish these goals, section 363(b) of the Bankruptcy Code provides "[t]he trustee after notice and a hearing, may use, sell, or lease, other than in the ordinary course of business, property of the estate." 11 U.S.C. § 363(b)(1). Courts have properly relied on section 363(b)'s broad authority to allow debtors in possession to pay prepetition claims in circumstances where, as here, the estate will obtain more value for all creditors or avoid more harm by making the prepetition payment. See In re Synteen Tech., Inc., No. 00-02203-W, 2000 WL 33709667, *2 (Bankr. D.S.C. 2000); In re Ionosphere Clubs, Inc., 98 B.R. 174,176-77 (Bankr. S.D.N.Y. 1989).

20. Moreover, section 105(a) of the Bankruptcy Code provides that "the court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." The purpose of Section 105(a) is to assure that the bankruptcy court has power to take whatever action is appropriate or necessary in aid of the exercise of its jurisdiction. 2 Collier on Bankruptcy ¶ 105.01 (15th ed. rev. 2004).

21. Numerous courts have used their section 105(a) equitable powers under the necessity of payment doctrine⁵ to authorize payment of a debtor's prepetition obligations where, as here, such payment is necessary to effectuate the "paramount purpose" of chapter 11 reorganization, which is to prevent the debtor from going into liquidation and preserve the

⁵ This doctrine, first articulated by the United States Supreme Court in Miltenberger v. C. & S.W.R. Co., 106 U.S. 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.

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 176.⁶

22. As is set forth in the Lodge Affidavit, authorizing, but not requiring, the Debtors to perform their pre-Petition Date obligations owed to the Dealers in order to maintain the Debtors' business relationships with the Dealers will enable the Debtors to maintain their

⁶ 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 Dealers in the instant case where significant value is derived from making such payments and there is a substantial likelihood that in the absence of such payments the Dealers can and will discontinue their services. See In re Kmart Corp., 359 F.3d 866 (7th Cir. 2004). Furthermore, the Debtors believe that they may assume the Dealer agreements and that the payment of prepetition amounts to the Dealers would constitute cure obligations in that event and are thus distinguishable from the contested payments in Kmart.

vast network of retail locations and to continue to enlist new subscribers and retain the Debtors' existing subscribers. If the Dealers are not timely paid it is likely that they will no longer be willing to provide services to the Debtors and/or the quality of their services will deteriorate. Due to the scarcity of available retail options in rural locations, which comprise the Debtors' only DIRECTV programming service territories, the loss of the Dealers would irreparably damage the Debtors' ability to reach its customer base. Moreover, any burden to the estate to pay such obligations is significantly outweighed by the resulting loss of business that would be caused by a failure to pay such obligations and the deleterious effects on the Dealers and customers. By reason of the importance of the Dealers to the Debtors' overall geographic presence and operations, the Debtors believe that paying such pre-Petition Date claims to the Dealers is integral to the Debtors' business going forward and their ability to maintain their enterprise value and to serve their customers. As a result, the Debtors submit that authorization to continue to operate in the ordinary course regarding the payment of pre-Petition Date amounts owed to Dealers is appropriate and justified under sections 363(b) and 105(a) of the Bankruptcy Code.

23. In addition, the claims against the Debtors resulting from non-payment of the prepetition amounts due under the Dealer programs would most likely constitute "cure" obligations under section 365(b)(1)(A) of the Bankruptcy Code to the extent the Debtors' contractual relationships with the Dealers are executory contracts that the Debtors could assume in the exercise of their business judgment. At this early stage of the bankruptcy case, the Debtors believe they would be permitted under section 365 to assume such contracts. However, rather than take such an action at this time, the Debtors propose to continue the status quo by paying the prepetition amounts due under the Dealer programs as set forth herein. Then, after

the Debtors have had the opportunity to review their executory contracts and develop a plan of reorganization, the Debtors can determine which of their contracts they wish to assume.

24. Finally, the Debtors submit that their ability to continue to operate in the ordinary course with respect to the Dealer programs is warranted under section 363(c)(1) of the Bankruptcy Code. Section 363(c)(1) provides that a debtor in possession “may enter into transactions, including the sale or lease of property of the estate, in the ordinary course of business, without notice or a hearing, and may use property of the estate in the ordinary course of business without notice or a hearing.” See In re Three Partners, Inc., 199 B.R. 230, 236 (Bankr. D. Mass. 1995) (explaining that 363(c)(1) applies so long as the business of the debtor is authorized to be operated under the Bankruptcy Code and discussing the limitations of section 363(c)(1)). Section 363(c)(1) is intended to give a debtor in possession “the flexibility to engage in ordinary transactions without unneeded oversight by creditors or the court, while at the same time giving creditors an opportunity to contest those transactions that are not ordinary.” In re Crystal Apparel, Inc., 207 B.R. 406, 409 (S.D.N.Y. 1997); In re Roth American, Inc., 975 F.2d 949, 952 (3rd Cir. 1992) (explaining that section 363(c)(1) strikes a balance between the debtors ability to carry on with its daily operations without excessive oversight and the need to protect secured creditors from the dissipation of assets); In re Sieling Assocs. Ltd. P’ship, 128 B.R. 721, 724 n.3 (Bankr. E.D. Va. 1991) (explaining that section 363(c)(1) allows a debtor in possession to ‘exercise reasonable judgment in carrying out its everyday affairs and . . . avoid excessive judicial involvement in it reorganization.’) (citing In re D’Lites of America, Inc., 108 Bankr. 352, 355 (Bankr. N.D. Ga. 1989)).

25. As set forth above, payment of the pre-Petition Date amounts owed to the Dealers is necessary and in the best interests of the Debtors, their estates, creditors, and other

parties-in-interest. In addition, the Debtors ability to reorganize will be seriously, if not irreparably, damaged unless the Debtors continue to maintain their existing relationships with the Dealers. The maintenance of these relationships depends on the payment of Dealer claims as set forth herein. Payment of the Debtors' pre-petition obligations to the Dealers is thus necessary to the survival of the Debtors and appropriate given the nature of the Debtors' reorganization efforts.

26. Nothing in this Motion should be construed as an assumption of any executory contract or unexpired lease between the Debtors and any of their Dealers, nor should it be construed as a rejection of any executory contract or unexpired lease. Furthermore, the Debtors reserve the right to contest the amount claimed to be due by any of the Dealers in the ordinary course of business.

NOTICE

27. 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

28. No previous application for the relief requested herein has been made by the Debtors to this or any other court

WHEREFORE, the Debtors respectfully request that the Court enter an order (i) granting the relief requested herein and (ii) granting such other and further relief as is just and proper.

Dated: Portland, Maine
June 2, 2004

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