

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

SECURITIES ACT OF 1933
Release No. 8653 / January 11, 2006

SECURITIES EXCHANGE ACT OF 1934
Release No. 53100 / January 11, 2006

ACCOUNTING AND AUDITING ENFORCEMENT
Release No. 2362 / January 11, 2006

ADMINISTRATIVE PROCEEDING
File No. 3-12146

In the Matter of

**Pegasus Satellite
Communications, Inc., and**

**Pegasus Media &
Communications, Inc.**

Respondents.

**ORDER INSTITUTING CEASE-AND-DESIST
PROCEEDINGS, MAKING FINDINGS, AND
IMPOSING A CEASE-AND-DESIST ORDER
PURSUANT TO SECTION 8A OF THE
SECURITIES ACT OF 1933 AND SECTION
21C OF THE SECURITIES EXCHANGE ACT
OF 1934**

I.

The Securities and Exchange Commission (“Commission”) deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted, pursuant to Section 8A of the Securities Act of 1933 (“Securities Act”) and Section 21C of the Securities Exchange Act of 1934 (“Exchange Act”), against Pegasus Satellite Communications, Inc. (“PSC”) and Pegasus Media & Communications, Inc. (“PM&C”) or collectively the “Respondents.”

II.

In anticipation of the institution of these proceedings, Respondents have submitted Offers of Settlement (the “Offers”) which the Commission has determined to accept. Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission is a party, and prior to a hearing pursuant to the Commission’s Rules of Practice, 17 C.F.R. § 201.100 et seq., and without admitting or denying the findings herein, except as to the Commission’s jurisdiction over them and the subject matter of these proceedings, which are admitted, Respondents consent to the entry of this Order Instituting Cease-and-Desist Proceedings, Making Findings, and Imposing a Cease-and-Desist

Order Pursuant to Section 8A of the Securities Act of 1933 and Section 21C of the Securities Exchange Act of 1934 (“Order”), as set forth below.

III.

On the basis of this Order and Respondents’ Offers, the Commission finds¹ that:

Respondents

1. PSC was a Delaware corporation with corporate headquarters in Bala Cynwyd, Pennsylvania. Through its operating subsidiaries, PSC operated broadcast television systems and provided direct broadcast satellite television services to customers in certain rural areas of the United States.

2. PM&C was a Delaware corporation with corporate headquarters in Bala Cynwyd, Pennsylvania, which together with its subsidiaries owned and operated broadcast television systems in exclusive territories primarily within rural areas of 41 states.

3. Respondents filed quarterly and annual reports with the Commission on Forms 10-Q and 10-K through June of 2004. PSC filed registration statements that incorporated these annual and quarterly reports on Forms S-4 through May 2001.²

Summary

This is a reporting and disclosure matter. Respondents inflated their publicly reported subscriber counts. They did so by including the accounts of customers whose accounts were or should have otherwise been de-activated. Because the subject accounts were not receiving services or making payments to the Respondents, the Respondents effectively increased the number of subscribers reported in press releases and in quarterly and year-end filings issued by the Respondents and filed with the Commission on Forms 10-Q and 10-K during, at least, 1999 to 2001. Reported subscriber numbers are a key performance measure by which investors and analysts evaluated companies operating in the satellite television business. On June 2, 2004, PSC, PM&C, and their subsidiary Pegasus Satellite Television, Inc. (“PST”), among other affiliates, filed voluntary petitions for relief under Chapter 11 of the United States Bankruptcy Code in the Bankruptcy Court for the District of Maine.³

¹ The findings herein are made pursuant to Respondents’ Offers of Settlement and are not binding on any other person or entity in this or any other proceeding.

² Until the completion of a reorganization in 2001, PSC was required to file periodic reports with the Commission under Section 13(a) of the Exchange Act as a result of registering securities pursuant to Section 12(g) of the Exchange Act. During the relevant time, PM&C was not subject to the Exchange Act’s reporting requirements, but did file reports on a voluntary basis. However, PM&C was still subject to the antifraud provisions of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder for false statements contained in those reports.

³ In re Pegasus Satellite Television, Inc. et al., Case No. 04-20878 (U.S. Bankr. D. Me.)

Respondents' Billing Practices

PSC and PM&C billed their customers through a billing system maintained by a telecommunications cooperative. The system generated subscriber statistics that were used to prepare reports. The system used certain criteria to determine which accounts would be considered active and included in the subscriber statistics and which accounts would be considered dropped, or "churned," and excluded from subscriber statistics. Under this system, a customer bill was generated one day after activation and was payable 21 days thereafter. The subscriber record keeping system automatically cut off and marked as churned accounts that were overdue by 54 days. Such churned accounts were not counted as part of the reportable subscriber base. The system also churned accounts with a zero balance that were not receiving services.

Respondents' Conduct

During at least 1999 through 2001, Respondents knowingly or recklessly implemented certain adjustments to inflate the number of active subscribers to their satellite television services as reported in their public filings. Personnel associated with the Respondents in at least two ways overrode features of the subscriber billing system that would have deemed certain accounts to be inactive or churned. Respondents "re-aged" certain accounts by extending them beyond the 54 day limit. This was done by manual intervention that overrode the automatic system cut-off features. In addition, Respondents kept certain accounts out of the churn category by assigning penny-credits to otherwise churned accounts. By these means, the Respondents added to their so-called "no-core" accounts—which were accounts that did not receive standard television packages and remained active as part of the publicly reported subscriber count.

PSC and PM&C typically reported the inflated subscriber numbers at or near the end of quarterly or annual reporting periods. For example, on June 26, 2000, four days before the June 30 end of the second quarter of that year, PST added approximately 2,400 subscribers to its active accounts by moving those accounts from the suspended category to the active category on its books and records. By issuing penny-credits to these accounts, PST was able to activate the accounts for reporting purposes. PST repeated this conduct on September 7 and 8, 2001, prior to the September 30 end of the third quarter of that year, when it moved approximately 1,042 and 950 accounts, respectively, from churn status to active status by use of penny-credits. Similar actions occurred on numerous other occasions throughout the period between 1999 and December 2001.

In the periodic reports then filed with the Commission, PSC and PM&C reported the number of subscribers for any given reporting period. In each quarterly and annual filing on Forms 10-Q and 10-K during the reporting periods from the third quarter of 1999 through December 2001, PSC and PM&C disclosed the number of its subscribers and attributed increases in subscriber numbers to, among other things, "internal growth." Neither PSC nor PM&C ever explained that a portion of their subscriber base consisted of "no-core" accounts. In their Forms 10-K for the year 2001, which contained virtually identical disclosures, PSC and PM&C reported 1,519,000 subscribers, compared to 1,403,000 for the prior year. In the same reports, PSC and PM&C stated that the year-to-year increase "was substantially due to internal growth." PSC and PM&C omitted to mention that the internal growth each cited included some non-core

subscribers that were activated by various means including the re-aging of accounts and the issuance of penny-credits as described above.

Stock analysts and public investors typically focused on subscriber numbers as one of the most important performance metrics for a company operating a satellite television business. Analysts' reports issued during the time subscriber numbers were inflated often cited those inflated numbers as part of the basis for their investment recommendations regarding PSC, PM&C and their affiliate companies.

In February 2002, PSC's management and audit committee undertook a review of the method by which it publicly reported the number of its subscribers.

In their 2001 10-Ks filed with the Commission on April 3 and April 9, 2002, respectively, PSC and PM&C announced that:

Our publicly reported subscriber counts in the past have included a number of accounts whose service has been suspended for prolonged periods of time. Because we believe it would improve our public reporting and internal analyses, we are changing our method of reporting subscribers, beginning with the first quarter of 2002 so as to exclude these accounts. We estimate that if we had instituted this change at December 31, 2001, we would have reported approximately 1.4 million subscribers.

Legal Discussion

The elements of fraud under Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, are, in general: (1) a device, scheme, or artifice to defraud or misstatements or omissions of material fact; (2) made in connection with the offer, sale, or purchase of securities; where (3) the defendants acted with scienter. The Supreme Court has defined scienter as a "mental state embracing intent to deceive, manipulate or defraud." *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976). The scienter requirement may also be met by recklessness. *In Re The Lesley Fay Companies, Inc.*, 871 F. Supp. 686 (S.D.N.Y. 1995) (explaining the evolution of recklessness to establish scienter). Courts have held that an issuer's public dissemination of materially false or misleading information through the press or in public filings with the Commission combined with public trading in the issuer's securities satisfy the nexus requirement of Section 10(b), and that selling or offering securities in the midst of a fraud, with knowledge of the fraud, violates Section 17(a). *S.E.C. v. Texas Gulf Sulphur Co.*, 401 F.2d 833 (2d. Cir. 1968) (*en banc*), *cert. denied*, 394 U.S. 976 (1969). *See also*, *S.E.C. v. Savoy Indus.*, 587 F.2d 1149, 1171 (D.C.Cir. 1978), *cert denied*, 440 U.S. 913 (1979).

Section 13(a) of the Exchange Act requires all issuers whose securities are registered with the Commission pursuant to Section 12 of the Exchange Act to file with the Commission periodic reports containing information prescribed by Commission rules and regulations. Pursuant to Section 13(a), the Commission has promulgated Rules 13a-1 and 13a-13, which require issuers to file annual and quarterly reports, respectively. Rule 12b-20 requires periodic reports to contain any additional information necessary to ensure that statements in the reports are not, under the circumstances, materially misleading. The filing of reports containing

materially false or misleading information constitutes a violation of the reporting provisions of the federal securities laws. *See, e.g., Savoy Indus.*, 587 F.2d at 1165. A showing of scienter is not required to establish liability under the reporting provisions. *Id.* at 1167.

Section 13(b)(2)(A) of the Exchange Act requires issuers to keep books, records, and accounts that, in reasonable detail, accurately and fairly reflect company transactions and the disposition of assets. Section 13(b)(2)(B) of the Exchange Act requires an issuer to “devise and maintain a system of internal accounting controls” that is sufficient to provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in conformity with generally accepted accounting principles and to maintain accountability for assets. Rule 13b2-1 of the Exchange Act prohibits any person from directly or indirectly falsifying any book, record or account required to be kept pursuant to Section 13(b)(2)(A) of the Exchange Act. Violations of Sections 13(b)(2)(A) and 13(b)(2)(B) do not require a showing of materiality or scienter. *S.E.C. v. Worldwide Coin Investments, Ltd.*, 567 F. Supp. 724, 749-51 (N.D. Ga. 1983).

IV.

As a result of the conduct described above, PSC violated Section 17(a) of the Securities Act, Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13 and 13b2-1 thereunder. As a result of its conduct described above, PM&C violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

V.

Undertakings

In determining to accept the Respondents’ Offers, the Commission further considered the following undertakings by Respondents. Ongoing Cooperation: Respondents shall cooperate fully with the Commission in any and all investigations, litigations or other proceedings relating to or arising from the matters described in the Order. In connection with such cooperation, Respondents have undertaken to produce promptly, without service of a notice or subpoena, any and all documents and other information requested by the Commission’s staff.

VI.

Accordingly, it is hereby ORDERED that:

PSC cease and desist from committing or causing any violations and any future violations of Section 17(a) of the Securities Act and Sections 10(b), 13(a), 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-13 and 13b2-1 thereunder.

PM&C cease and desist from committing or causing any violations and any future violations of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

By the Commission.

Nancy M. Morris
Secretary