

**Before the
Federal Communications Commission
Washington, DC 20554**

In the Matter of)	
)	
Schools and Libraries Universal Service)	CC Docket No. 02-6
Support Mechanism)	DA 12-1325

**Comments of Jive Communications, Inc. on the Petition Filed by the
State E-Rate Coordinators' Alliance**

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**Comments of Jive Communications, Inc. on the Petition Filed by the
State E-Rate Coordinators' Alliance**

Jive Communications, Inc. (“Jive”) hereby submits these comments in response to the Public Notice (the “Public Notice”) issued by the Wireline Competition Bureau (“Bureau”) in the above-captioned proceeding seeking comments on the Petition filed by the State E-Rate Coordinators’ Alliance, which requested clarification regarding the eligibility of bundled end user equipment under the Schools and Libraries Universal Service Support Mechanism (“E-Rate”).¹

Introduction and Summary

In these comments, Jive urges the Commission to reaffirm the Bureau’s statements in the *Clarification Order*, and direct USAC to process the applications that implicate this policy now pending with the Schools and Libraries Division (“SLD”).

Founded in 2006, Jive is a provider of interconnected Hosted Voice over Internet Protocol (“VoIP”), among other services, to institutional and enterprise customers. Jive began participating in the E-Rate program for FY 2010, and its E-Rate business has grown steadily since that time. For FY 2012, Jive is the service provider named in 154 funding requests spanning 26 states and totaling over \$6.2 million.

¹ Public Notice, CC Docket No. 02-6, *Wireline Competition Bureau Seeks Comment on a Petition Filed by the State E-Rate Coordinators’ Alliance Seeking Clarification regarding the Eligibility of Bundled End User Equipment under the Schools and Libraries Program*, DA 12-1325 (Wir. Comp. Bur. rel. Aug. 10, 2012).

Jive offers its Hosted VoIP services to institutional and other enterprise customers in conjunction with a selection of Cisco and Polycom handsets and related hardware. After careful examination of the Commission's *Sixth Report and Order*,² the Bureau's *Clarification Order*,³ and USAC's response to Jive's submission for clarification to USAC's Client Services Bureau, in 2012, Jive began offering customers that purchase Jive Hosted VoIP service with a 36-month term commitment access to a limited selection of free handsets to use with the service. Customers that do not make the 36-month service commitment must purchase the handsets separately, but receive the same rate for Jive's Hosted VoIP services as similar customers making the 36-month term commitment. Jive makes these offers available to all of its institutional or enterprise customers, including E-Rate applicants, without distinction. Based on Jive's understanding, its competitors structure their product and service offerings in a similar manner. Indeed, it has become standard in the industry for providers to offer free VoIP handsets (or cell phones) to customers that commit to a multi-year contract.

Jive began marketing its 36-month service offering, including the free handsets, to schools and libraries following publication of the *Clarification Order*, which implemented certain language in the Commission's *Sixth Report and Order* by limiting the application of the cost allocation requirements to cases where service providers "offer special equipment discounts or equipment with service arrangements to E-rate recipients that are not currently available to

² *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Sixth Report and Order, FCC 10-175, 25 FCC Rcd 18762 (2010) ("*Sixth Report and Order*").

³ *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Order, DA 10-2355, 25 FCC Rcd 17324 (Wir. Comp. Bur. 2010) ("*Clarification Order*").

some other class of subscribers or segment of the public.”⁴ Thus, in doing so, the Bureau offered as an example that:

[M]any cell phones are free or available to the general public at a discounted price with the purchase of a two-year service contract. Schools and libraries are free to take advantage of these deals, without cost allocation, but cannot accept other equipment with service arrangements that are not otherwise available to some segment of the public or class of users. Therefore, a service provider may not offer free iPads to a school with the purchase of telecommunications or Internet access services eligible under E-rate, if such an arrangement is not currently available to the public or a designated class of subscribers.⁵

Since the Bureau released the *Clarification Order*, USAC and E-Rate program participants alike have struggled to understand the precise scope and implementation of this policy refinement, which these comments will call the “Free Handset Policy.”⁶ Its request for clarification notwithstanding, USAC has nevertheless moved to implement this policy by modifying its Free Services Advisory to indicate, consistent with the *Clarification Order*, that a “cost allocation is not required when the free product or service is available to the public or a class of subscribers broader than just E-rate recipients.”⁷

⁴ *Clarification Order* at ¶ 11.

⁵ *Id.* at ¶ 11 n. 25.

⁶ *See, e.g.*, State E-Rate Coordinators Alliance, Petition for Clarification Pertaining to the Eligibility of Free VoIP Handsets and Other End-User Equipment, CC Docket No. 02-6, GN Docket No. 09-51 (filed July 27, 2012) (“SECA Petition”); Letter from Mel Blackwell, Vice President, Schools and Libraries Division, to Sharon Gillett, Chief, Wireline Competition Bureau, “Request for Guidance on Rules Governing Gifts in the E-rate Program,” CC Docket No. 02-6 (filed Aug. 5, 2011) (“USAC Letter”).

⁷ *See* “Free Services Advisory,” available at: <http://usac.org/sl/applicants/step02/free-services-advisory.aspx>.

Discussion

A. The Clarification Order Articulated a Clear and Workable Implementation of the Commission's Sixth Report and Order Policy

In articulating the Free Handset Policy, the Bureau did not cite a specific portion of the *Sixth Report and Order*. Nevertheless, Jive believes that the Bureau's actions were intended to clarify the boundaries of the new *Sixth Report and Order* rules governing the giving of gifts from service providers to E-Rate applicants.⁸ Explaining the limits of the new gift rules contained in the *Sixth Report and Order*, the Commission stated that:

If contributions have no relationship to the procurement of E-rate eligible services and are not given by service providers to circumvent our rules, including rules that require schools and libraries to pay their own non-discount share for the services they are purchasing, such contributions will not violate the prohibition against gift-giving.”⁹

The *Clarification Order* thus supplied a bright line test to illustrate the circumstances in which the Commission would view a contribution of equipment to an E-Rate applicant as having “no relationship to the procurement of E-Rate eligible services.” That is, in cases where the “gift” of equipment is generally available to the public, or to some segment of non-E-Rate customers, on similar terms and conditions, then it cannot be viewed as a prohibited gift intended to influence the procurement specifically of E-Rate services, any more than such a “gift” of a free or discounted handset is intended to influence any other consumer's decision to purchase the telecommunications services it supports.

The Commission's *Sixth Report and Order* and Bureau's *Clarification Order* removed a disadvantage faced by E-rate applicants in comparison to other market segments with respect to

⁸ *Sixth Report and Order* at ¶¶ 87-90.

⁹ *Sixth Report and Order* at ¶ 90.

their receipt of such free equipment. The Commission's cost allocation rule, as previously in effect, required cost allocation between eligible Priority One services and ineligible equipment, even if free, provided in connection with those services.¹⁰ Thus, the rule prevented E-Rate applicants uniquely from taking full advantage of the practice, common in the telecommunications industry, of providing free equipment with the purchase of telecommunications service.

B. The Free Handset Policy Is a Logical Outgrowth of the Commission's Cost Allocation Rules

The *Clarification Order's* explanation that cost allocation is only required where applicants take "special equipment discounts or equipment with service arrangements to E-rate recipients that are not currently available to some other class of subscribers or segment of the public"¹¹ is a logical outgrowth of the Commission's longstanding cost allocation rules, including the "ancillary use" policy. The Commission's cost allocation rule is intended to "improve[e] each school or library's ability to purchase the most useful and cost-effective service."¹² Under that rule, when a product or service has mixed eligibility, that is, some features or functions are E-rate-eligible and some are not, then the applicant or service provider may submit a cost allocation that separates the eligible and ineligible portions. Under the cost allocation rules, the cost allocation chosen by the applicant must have a tangible basis and the

¹⁰ 47 C.F.R. § 54.504(e); *see also* USAC: Free Services Advisory, available at: <http://www.usac.org/sl/applicants/step02/free-services-advisory.aspx> (last visited Aug. 6, 2012) ("Applicants and service providers are prohibited from using Schools and Libraries Program support to subsidize the procurement of ineligible or unrequested products and services or from participating in arrangements that have the effect of providing a discount level to applicant(s) greater than that to which the applicant(s) are entitled.").

¹¹ *Clarification Order* at ¶ 11.

¹² *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Third Report and Order and Second Further Notice of Proposed Rulemaking, FCC 03-323, 18 FCC Rcd 26912 ¶ 38 (2003) ("*Third Report and Order*").

price for the eligible portion must be the most cost effective means of receiving the eligible service.¹³ An exception permits applicants to receive support without performing cost allocation when the ineligible component is considered “ancillary” to the overall package.¹⁴ To be considered “ancillary,” it must not be possible to determine the price of the ineligible component separately and independently from the price of the eligible components, and the package must represent the most cost-effective means of receiving the eligible services, without regard to the value of the ineligible functionality.¹⁵

As reflected in the “ancillary use” rule, the Commission should tailor its cost allocation requirements as narrowly as possible to achieve their intended purposes, (1) to protect the integrity of the Commission’s E-Rate procurement rules; and (2) to ensure that ineligible components do not unreasonably burden the fund. The Free Handset Policy amply meets these goals. By limiting the exception to those cases where free equipment is on offer to broader classes of customers beyond the community of E-Rate applicants, the policy ensures that the free equipment is neither being used to influence the procurement process, nor likely to create an

¹³ See 47 C.F.R. § 54.504(e)(1) (“*Ineligible components*. If a product or service contains ineligible components, costs must be allocated to the extent that a clear delineation can be made between the eligible and ineligible components. The delineation must have a tangible basis, and the price for the eligible portion must be the most cost-effective means of receiving the eligible service.”); *Third Report and Order*, at ¶¶ 36-39.

¹⁴ 47 C.F.R. § 54.504(e)(2) (“If a product or service contains ineligible components that are ancillary to the eligible components, and the product or service is the most cost-effective means of receiving the eligible component functionality, without regard to the value of the ineligible component, costs need not be allocated between the eligible and ineligible components. Discounts shall be provided on the full cost of the product or service. An ineligible component is “ancillary” if a price for the ineligible component cannot be determined separately and independently from the price of the eligible components, and the specific package remains the most cost-effective means of receiving the eligible services, without regard to the value of the ineligible functionality.”).

¹⁵ *Id.*

unreasonable burden on the fund, given that such packages are designed to have commercial appeal in the larger market.

In this way, the Free Handset Policy is a modest extension of the current “ancillary use” rule. As with the “ancillary use” rule, it is difficult to determine a meaningful standalone price for the ineligible equipment. Although free equipment included in E-Rate contracts might nominally be sold on a standalone basis and, therefore, have an established market price, it is also clear that the lines between the equipment and the service sold in packages are increasingly blurred. Particularly in the mobile wireless industry, service providers frequently have exclusive rights to certain handsets, which manufacturers have optimized for use on their networks; these handsets are “locked” to prevent use with other providers’ service; and, even in cases where the carrier is willing to “unlock” the handset, today’s diversity of frequency bands and transmission standards are likely to limit the handset’s ability to function using other providers’ services in any event. The market pricing of equivalent “unlocked” handsets available from the handset manufacturer is equally unavailing; unlocked handsets offer the user a level of worldwide geographic flexibility in selecting and using communications services that make them attractive to an entirely different customer from the buyer of a package that includes a particular provider’s services and a locked handset.

As with the ancillary use rule, the package price is frequently the most cost effective way to obtain the eligible service, without regard for the ineligible components. Not only is the complete package of components (*i.e.*, handset and service) required for the service to function, standalone handset pricing is nearly always designed to reward the customer willing to make a term commitment to the service provider. The monthly recurring charges for Jive’s services, for

example, are identical for month-to-month customers and those signing a three-year commitment.¹⁶

Indeed, this pricing strategy exposes the fundamental flaw in the Commission's cost allocation rules that the Free Handset Policy alleviates. The Commission's cost allocation rules are built on the premise that, in general, where the eligible and ineligible components of a package may be purchased separately, the eligible components will cost somewhat less than the price of the package to purchase on a standalone basis, even if the package price represents a savings when compared to the sum of the individual component prices. Under this theory, at first glance, it appears possible, not only to quantify the "savings," but to allocate it meaningfully among the eligible and ineligible components.

Whatever the merit of such an approach might be when applied to packages of goods, it rapidly breaks down when applied to packages that mix goods and services. When Jive provides handsets for free to customers who also make a term commitment for service, the overall monthly cost of service is identical to that charged to customers not making such a commitment. The cost to Jive of providing this incentive is not measured by the retail price of the equipment, but by its wholesale cost of obtaining that equipment. Moreover, the cost is offset by other economic factors involved in the customer relationship, such as a reduction in customer acquisition and retention costs over the course of the contract term, and Jive's willingness to accept a lower margin of return in exchange for the predictability of a committed revenue stream.

¹⁶ Similarly, AT&T and Verizon Wireless both offer the iPhone 4S, a popular model, at a \$450 discount for customers willing to sign a two-year contract, as compared to the "no commitment" price. *See*, <https://www.att.com/shop/wireless/devices/apple/iphone/4s-16gb-black.html>; <http://www.verizonwireless.com/b2c/store/controller?item=phoneFirst&action=viewPhoneDetail&selectedPhoneId=5776>. Because the pricing of service plans necessary to use the handset is identical in either case, this represents a savings of nearly \$20 per month over the term of the contract.

C. SECA's Proposed Limitations Would Confuse, not Clarify, the Scope and Application of the Free Handset Policy

In connection with its comments on the Commission's FY 2013 Eligible Services List,¹⁷ Jive cautioned that the Commission should carefully consider the additional limiting criteria that SECA had proposed to limit application of the Free Handset Policy before adopting such further limitations could induce still further questions and uncertainty. In light of the discussion above, Jive believes that the Commission should direct SLD to proceed by processing pending applications that implicate the Free Handset Policy, and address any implementation issues as they arise through the existing processes for assisting applicants, conducting diligence on funding requests, and resolving Requests for Review.

In its Petition, SECA asks for clarification that the scope of the Free Handset Policy is limited to the following circumstances:

- The cost of any end-user equipment provided as a part of a bundled service must be considered "ancillary" relative to the cost of the bundle as a whole;
- The bundled service offering must be deemed a commercially common practice within the industry, not a unique offering of an individual service provider;
- The arrangement must be currently available to the public and not just to a designated class of subscribers. For example, a special bundle available only to the K-12 market that is not available to all other customers should not qualify for the cost allocation exemption; and
- The service provider is not permitted to offer a package or packages of equivalent eligible services, without bundled end-user equipment, at a lower price.¹⁸

Jive shares SECA's belief that the E-Rate rules should be as clear and carefully drawn as possible. Because USAC lacks the authority to make E-Rate rules or discretion to depart from

¹⁷ *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Comments of Jive Communications, Inc. (filed Aug. 6, 2012) ("Jive ESL Comments"), attached hereto as **Exhibit A**.

¹⁸ SECA Petition at 3.

Commission policies, the Commission must strive to state its E-Rate rules and policies as clearly as possible, minimizing opportunities for confusion or misinterpretation of Commission intent.

As indicated in the Jive ESL Comments, while the SECA Petition reflects some thoughtful consideration of whether limits are needed to ensure that the Free Handset Policy does not swallow the Commission's general cost allocation rule, adoption of the SECA criteria would raise at least as many implementation issues as it would resolve.

Specifically, SECA's first suggestion – to limit application of the Free Handset Policy to situations in which the free ineligible products or services are “ancillary” – closely resembles the Commission's existing “ancillary use” rule, discussed above.¹⁹ Of course, to the extent that a free handset or other piece of equipment met the ancillary use test, no cost allocation would be required at all, and the Free Handset Policy would be reduced to a nullity. To the extent that SECA advocates sole focus on the magnitude of the cost of the equipment, or a requirement that the equipment cannot be priced separately, Jive believes that this focus departs from the Commission's intent, as manifested in the example of a mobile phone offered in the *Clarification Order*.

With respect to cost effectiveness, as discussed above, many handsets that are nominally priced and offered for sale on a standalone basis are nevertheless nearly always actually sold in far more cost effective packages with monthly services. Given that many of these handsets are locked and have only limited functionality on competing networks, such nominal standalone equipment offerings verge on irrelevance, and offerings of unlocked handsets offer sufficiently

¹⁹ 47 C.F.R. § 54.504(e)(2) (“An ineligible component is ‘ancillary’ if a price for the ineligible component cannot be determined separately and independently from the price of the eligible components, and the specific package remains the most cost-effective means of receiving the eligible services, without regard to the value of the ineligible functionality.”).

different capabilities that they cannot be used to establish a market price. Nevertheless, Jive's practices and those of other service providers are consistent with this requirement, and Jive would not object application of this second ancillary criterion applied to the Free Handset Policy if the Commission believed that additional requirement to be essential.

With respect to SECA's second criterion – “commercially common practice within the industry” – Jive again would urge caution in implementing this or any similar criterion. Nothing in the *Sixth Report and Order* or *Clarification Order* suggests that this refinement to the cost allocation policy should be limited to cases where the practice is common within the industry. Moreover, Jive believes that neither the Commission nor USAC is well positioned to become the arbiter on an ongoing basis of which commercial practices have emerged as “common.” For example, it was once “common,” for local telephone companies to require their customers to lease customer premises equipment (“CPE”) at monthly tariffed rates for use with their service. Even after the Commission deregulated CPE, many customer chose to continue this arrangement, sometimes for decades, and the point at which it ceased to be “common” is at least as much a question of art as science. By tying E-Rate support to such a determination, the Commission would substantially retard the continually evolving and vibrant communications technology industry's ongoing efforts to incorporate new technologies and more effective pricing models into creative solutions that meet customer needs. The Commission should not impose such preferential treatment for legacy solutions over new solutions, and such an approach in fact is not necessary to provide the desired clarity in the Commission's policy.

The third SECA criterion – “available to the public” – again raises implementation issues and appears to directly contravene clear language in the *Clarification Order*. In order to fall within the Free Handset Policy, the *Clarification Order* states that the equipment must be

available to “some other class of subscribers or segment of the public.”²⁰ SECA’s proposal to limit the scope of the *Clarification Order* to offers that are available to the public generally is overly narrow. While Jive agrees that an offer that is available generally to every member of the public would qualify, the *Clarification Order* establishes that offers to narrower classes of customers may do so as well.

Similarly, the *Clarification Order* appears readily to answer USAC’s query whether, “all libraries and elementary and secondary schools [may be] considered a ‘class of subscribers’ such that a special equipment discount or free equipment offered only to libraries and elementary and secondary schools would allow a school or library participating in the E-rate program to accept free or discounted equipment from a service provider.”²¹ The *Clarification Order* states that the offer must be available to “some *other* class of subscribers.” Jive believes that “other” in that sentence refers to E-Rate applicants. Therefore, even though Jive’s free handset offer is available to enterprise and public sector customers making a three-year service commitment, Jive believes that an offer limited to schools and libraries generally, without regard for whether they participate in E-Rate, should meet this test.

Finally, with respect to the fourth criterion – “no packages of equivalent eligible services, without bundled end-user equipment, at a lower price” – Jive generally agrees with this concept, but would urge the Commission to make clear that it applies only across similarly situated customers. In Jive’s experience, for example, it is entirely possible that pricing will vary with volume commitments in addition to term commitments, and it is likely that customers purchasing a large volume of services may receive lower unit pricing than smaller customers. These

²⁰ *Clarification Order* at ¶ 11.

²¹ USAC Letter, at 2-3.

variations have nothing to do with free equipment, but stem from well-recognized principles of cost causation, such as the relative economies of scale that service providers can bring to bear in serving larger volume customers, the complexity of the engagement, the level of competitive price pressure present in individual geographic markets, and other factors. The key consideration is that the selected package remain the most cost effective way to receive the eligible services, without regard for the ineligible components, regardless of whether the price is the lowest available to any customer, anywhere.

In short, therefore, Jive believes that the *Clarification Order* already provides a workable framework within which the Free Handset Policy may be applied, and believes that the Commission should direct SLD to move forward with decisions on pending funding requests. If the Commission provides any further clarification at this time, Jive suggests that it be limited to a requirement that the cost of the full service offering must be the most cost-effective means of receiving the eligible service, without regard to the value of the ineligible functionality. Further implementation issues, if any, should be addressed through subsequent prospective Orders and in the process of resolving Requests for Review that may implicate this issue. Jive believes that it is only through this “learning by doing” implementation process that the Commission, USAC, and E-Rate applicants and service providers will gain the clarity they seek.

Finally, the Commission should proceed in a manner that is mindful of the fact that the Free Handset Policy has been in effect now for nearly two years, since at least the December 2010 release of the *Clarification Order* and the September 2010 publication of the *Sixth Report and Order*. If the Commission determines that that is should issue clarifying changes to this policy that narrow the circumstances in which the policy applies, Jive urges the Commission to make such clarifications prospective in scope. For the past two years, service providers and

applicants alike have been entering into contractual business relationships that took the FCC, the Bureau, and USAC at face value when they established the Free Handset Policy. It would severely undermine the goals of the E-Rate program, ultimately to the detriment of the nation's school children, for the Commission to deny funding now after applicants and service providers acted in reliance on previous representations of the E-Rate program's regulators and administrators to the contrary.

D. The Commission Should Direct USAC to Process E-Rate Applications that Fall within the Scope of the *Clarification Order*

Currently, USAC appears to be withholding decisions on funding requests that involve "free" handsets, even though these funding requests are consistent with the Commission's refinement to its cost allocation policy. Jive urges the Commission to direct USAC to process applications now pending with the Schools and Libraries Division ("SLD") that implicate the Free Handset Policy. As discussed below, the statements regarding the treatment of free end user equipment in the *Clarification Order* are a proper interpretation of Commission policy established in the *Sixth Report and Order*; the Bureau's clarification established clear boundaries for this policy that can be readily implemented by USAC; and SLD has modified its Free Services Advisory to reflect this change, clearly a positive indication to the E-rate community that USAC understands the Commission's stated intent. . Despite these facts, E-Rate applicants that have availed themselves of this change have seen their applications languish, as SLD has declined to act.

SLD appears to have stopped processing applications that implicate the policy statements contained in the *Clarification Order* regarding free end user equipment after USAC submitted its

letter seeking further clarification of this policy more than a year ago.²² The SLD's delay is not only unwarranted, but also creates financial and operational hardships for applicants and service providers alike. FY 2012 is nearing the end of its first calendar quarter. Schoolchildren have returned to classes and, for them to receive the benefits the E-Rate program is intended to foster, the services E-Rate supports must be available. Yet, mindful of the harm that the applicant's educational mission sustains when services are not available during the entire Funding Year, applicants and service providers alike are forced to guess whether their applications will be successful. In making this guess, they must weigh this harm against the financial risks that funding uncertainty creates for both applicants and service providers, neither of whom may be in position to sustain the devastating financial impact of the loss of E-Rate funding late in a Funding Year, after the supported services have already been provided and the service provider has incurred the associated costs.

Rather than forcing applicants and service providers to choose between the educational interests of schoolchildren and the risk of financial cataclysm, SLD should provide timely decisions under Commission policy as it is then in effect. The Commission should therefore direct SLD to process applications that fall within the *Clarification Order's* treatment of free equipment, rather than continuing to harm E-Rate program applicants and service providers by imposing open-ended delay on its processing of their applications.

²² See USAC Letter.

Conclusion

For the foregoing reasons, Jive urges the Commission to reaffirm the Bureau's statements in the *Clarification Order* implementing the Free Handset Policy, and direct USAC to process the applications that implicate this policy now pending with SLD.

Respectfully submitted,

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September 10, 2012

EXHIBIT A

**Before the
Federal Communications Commission
Washington, DC 20554**

In the Matter of)	
)	
Schools and Libraries Universal Service Support Mechanism)	CC Docket No. 02-6
)	
A National Broadband Plan For Our Future)	GN Docket No. 09-51

**Comments of Jive Communications, Inc. on the Draft Eligible Services
List for the Schools And Libraries Universal Service Program**

Jive Communications, Inc. (“Jive”) hereby submits these comments in response to the Public Notice (the “Public Notice”) issued by the Wireline Competition Bureau (“Bureau”) in the above-captioned proceedings publishing the draft Eligible Services List (“ESL”) to govern funding commitments under the Schools and Libraries Universal Service Support Mechanism (“E-Rate”) for Funding Year (“FY”) 2013.¹

Introduction and Background

Founded in 2006, Jive is a provider of interconnected Hosted Voice over Internet Protocol (“VoIP”), among other services, to institutional and enterprise customers. Jive began participating in the E-Rate program for FY 2010, and its E-Rate business has grown steadily since that time. For FY 2012, Jive is the service provider named in 154 funding requests spanning 26 states and totaling over \$6.2 million.

Jive offers its Hosted VoIP services to institutional and other enterprise customers in conjunction with a selection of Cisco and Polycom handsets and related hardware. After careful

¹ Public Notice, CC Docket No. 02-6, GN Docket No. 09-51, *Wireline Competition Bureau Seeks Comment on Draft Eligible Services List for Schools and Libraries Universal Service Program*, DA 12-1052, 27 FCC Rcd 7405 (Wir. Comp. Bur. 2012).

examination of the Commission's *Sixth Report and Order*,² the Bureau's *Clarification Order*,³ and USAC's response to Jive's submission for clarification to USAC's Client Services Bureau, in 2012, Jive began offering customers that purchase Jive Hosted VoIP service with a 36-month term commitment access to a limited selection of free handsets to use with the service.

Customers that do not make the 36-month service commitment must purchase the handsets separately, but receive the same rate for Jive's Hosted VoIP services as similar customers making the 36-month term commitment. Jive makes these offers available to all of its institutional or enterprise customers, including E-Rate applicants, without distinction. Based on Jive's understanding, its competitors structure their product and service offerings in a similar manner. Indeed, it has become standard in the industry for providers to offer free VoIP handsets (or cell phones) to customers that commit to a multi-year contract.

Thus, in adopting new rules in the *Sixth Report and Order* to govern the giving of gifts from service providers to E-Rate applicants,⁴ the Commission also took the opportunity to remove a disadvantage faced by E-rate applicants in comparison to other market segments with respect to their receipt of free equipment, such as handsets or cell phones. The Commission's cost allocation rule, as previously in effect, required cost allocation between eligible Priority One services and ineligible equipment, even if free, provided in connection with those services.⁵

² *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Sixth Report and Order, FCC 10-175, 25 FCC Rcd 18762 (2010) ("*Sixth Report and Order*").

³ *Schools and Libraries Universal Service Support Mechanism*, CC Docket No. 02-6, Order, DA 10-2355, 25 FCC Rcd 17324 (Wir. Comp. Bur. 2010) ("*Clarification Order*").

⁴ *Sixth Report and Order* at ¶¶ 87-90.

⁵ 47 C.F.R. § 54.504(e); see also USAC: Free Services Advisory, available at: <http://www.usac.org/sl/applicants/step02/free-services-advisory.aspx> (last visited Aug. 6, 2012) ("Applicants and service providers are prohibited from using Schools and Libraries Program support to subsidize the procurement of ineligible or unrequested products and

Thus, the rule prevented E-Rate applicants uniquely from taking full advantage of this common industry practice.

The new Commission policy permits the inclusion of such end user components in E-Rate contracts without cost allocation if certain requirements are met. Explaining the limits of the new gift rules contained in the *Sixth Report and Order*, the Commission stated that, “[i]f contributions have no relationship to the procurement of E-rate eligible services and are not given by service providers to circumvent our rules, including rules that require schools and libraries to pay their own non-discount share for the services they are purchasing, such contributions will not violate the prohibition against gift-giving.”⁶

Implementing this language, the Bureau subsequently explained that the *Sixth Report and Order* limits the scope of the cost allocation requirements to cases where service providers “offer special equipment discounts or equipment with service arrangements to E-rate recipients that are not currently available to some other class of subscribers or segment of the public.”⁷ Based on this analysis, the Bureau offered as an example that:

[M]any cell phones are free or available to the general public at a discounted price with the purchase of a two-year service contract. Schools and libraries are free to take advantage of these deals, without cost allocation, but cannot accept other equipment with service arrangements that are not otherwise available to some segment of the public or class of users. Therefore, a service provider may not offer free iPads to a school with the purchase of telecommunications or Internet access services eligible under E-rate, if such an arrangement is not currently available to the public or a designated class of subscribers.⁸

services or from participating in arrangements that have the effect of providing a discount level to applicant(s) greater than that to which the applicant(s) are entitled.”).

⁶ *Sixth Report and Order* at ¶ 90.

⁷ *Clarification Order* at ¶ 11.

⁸ *Id.* at ¶ 11 n. 25.

Since that Bureau *Clarification Order* was issued, USAC and E-Rate program participants alike have struggled to understand the precise scope and implementation of this policy refinement.⁹ At present, USAC appears to be withholding decisions on funding requests that involve “free” handsets, even though these funding requests are consistent with the Commission’s refinement to its cost allocation policy.

Discussion

Amendments to the FY 2013 ESL. In these comments, Jive requests that the Commission incorporate language into the FY 2013 ESL to recognize the exception established by the Commission’s *Sixth Report and Order* and the Bureau’s *Clarification Order*¹⁰ to the cost allocation requirements contained in Section 54.504(e) of the Commission’s rules, 47 C.F.R. § 54.504(e) and the Free Services Advisory¹¹ published by the Universal Service Administrative Company (“USAC”), the Commission’s E-Rate program administrator.

Current uncertainty regarding the precise interplay between the cost allocation requirement and the *Clarification Order* is creating significant disruption for E-Rate applicants and service providers alike. Service providers, including Jive, are experiencing significant disruption to their businesses as a result of delays in obtaining funding commitments and

⁹ See, e.g., State E-Rate Coordinators Alliance, Petition for Clarification Pertaining to the Eligibility of Free VoIP Handsets and Other End-User Equipment, CC Docket No. 02-6, GN Docket No. 09-51 (filed July 27, 2012) (“SECA Petition”); Letter from Mel Blackwell, Vice President, Schools and Libraries Division, to Sharon Gillett, Chief, Wireline Competition Bureau, “Request for Guidance on Rules Governing Gifts in the E-rate Program,” CC Docket No. 02-6 (filed Aug. 5, 2011).

¹⁰ *Clarification Order* at ¶ 11 n. 25.

¹¹ USAC: Free Services Advisory, at <http://www.usac.org/sl/applicants/step02/free-services-advisory.aspx> (last visited Aug. 6, 2012) (“Applicants and service providers are prohibited from using Schools and Libraries Program support to subsidize the procurement of ineligible or unrequested products and services or from participating in arrangements that have the effect of providing a discount level to applicant(s) greater than that to which the applicant(s) are entitled.”).

disbursements. Applicants undoubtedly face uncertainty and substantial legal risk surrounding their evaluation and selection of bids they may receive in response to their Form 470 postings that include offers of free equipment that meets the circumstances described by the Bureau.

Going into the FY 2013 procurement cycle, it is critical that the Commission include clear guidance in the ESL to reflect the new limits on the need for cost allocation articulated in the *Sixth Report and Order* and *Clarification Order*. By doing so the Commission can avert countless disputes that will otherwise inevitably produce bid protests, funding delays, commitment adjustments, audit findings, and other costly compliance issues across the E-Rate program.

To avert these issues, at least with respect to FY2013, Jive therefore urges the Commission to adopt the following addition to page 7 of the draft FY 2013 ESL (addition shown in italics):

The following charges are **NOT ELIGIBLE** for E-rate support:

-End User Equipment. Support is not available for end-user equipment. E-rate applicants may, however, accept free end user equipment without cost allocation if the equipment offer is available to some other class of subscribers or segment of the public on the same terms and conditions, and the underlying service to which the equipment relates is the most cost effective without regard to the otherwise ineligible equipment components.

Jive believes that the free handsets it provides with a customer's 36-month commitment to its Hosted VoIP service offering fully meet this standard. Indeed, this structure is a specific implementation of the free mobile handset example offered by the Bureau in the *Clarification Order*. Jive offers free devices to any customer – E-Rate or otherwise – that signs a 36-month contract for its services. The price of the Hosted VoIP service is the same, regardless of whether the customer accepts this offer; in the case of shorter-term contracts, the customer pays no higher rate for service, but is required to purchase or lease the necessary equipment separately.

Further, the cost of Jive's Hosted VoIP services is lower today than it was even one year ago. Not only does this provide independent confirmation that Jive is not inflating service rates to

cover the cost of the free equipment, but it also conclusively shows that the 36-month commitment that includes free equipment is the most cost-effective way to purchase Jive services.

Preliminary Review of the SECA Petition. In its Petition, SECA asks for clarification that the scope of the Commission’s refinements to its cost allocation policy is limited to the following circumstances:

- The cost of any end-user equipment provided as a part of a bundled service must be considered “ancillary” relative to the cost of the bundle as a whole;
- The bundled service offering must be deemed a commercially common practice within the industry, not a unique offering of an individual service provider;
- The arrangement must be currently available to the public and not just to a designated class of subscribers. For example, a special bundle available only to the K-12 market that is not available to all other customers should not qualify for the cost allocation exemption; and
- The service provider is not permitted to offer a package or packages of equivalent eligible services, without bundled end-user equipment, at a lower price.¹²

Jive appreciates SECA’s thoughtful discussion of these issues and will file more fulsome comments if the Commission establishes a formal pleading cycle for the SECA Petition. Jive agrees that the Commission can and should further define the scope of the new cost allocation policy refinements, to ensure that the “cell phone” exception does not swallow the rule.

Nevertheless, Jive urges the Commission not to delay in amending the FY 2013 ESL as Jive requests above. Delaying such critical guidance would cause substantial harm to the E-Rate program, as described above, by allowing the “perfect to be the enemy of the good.”

In general, Jive believes that, while the SECA Petition offers a thoughtful starting point and would resolve some implementation issues, the criteria SECA proposes would also raise implementation issues of their own. For example, the first criterion – “ancillary cost” – bears an

¹² SECA Petition at 3.

uncertain relationship to the Commission's existing "ancillary use" rule.¹³ Of course, to the extent that a free handset or other piece of equipment met the ancillary use test, no cost allocation would be required at all. To the extent that SECA advocates sole focus on the cost of the equipment, or a requirement that the equipment cannot be priced separately, however, Jive believes that this focus departs from the Commission's intent, as manifested in the example of a mobile phone offered in the *Clarification Order*. Standalone pricing for end-user handsets is readily available for both mobile and VoIP equipment; thus adoption of this criterion could undermine the validity of the Bureau's example.

With respect to the second criterion – "commercially common practice within the industry" – Jive again would urge caution in implementing this or any similar criterion. Nothing in the *Sixth Report and Order* or *Clarification Order* suggests that this refinement to the cost allocation policy should be limited to cases where the practice is common within the industry. Furthermore, Jive is concerned that such a restriction could stifle creativity and development of new service offerings. While service providers commonly offer free mobile and VoIP handsets today to customers making a term commitment, industry practices evolve over time. The SECA Petition offers no definition of "common," nor does it explain how USAC would identify or communicate over time which marketing practices have emerged as "common" within the industry and therefore should be considered exempt from cost allocation.

The third criterion – "available to the public" – again raises implementation issues. The *Clarification Order* establishes that the free equipment offer must be available to "class of

¹³ 47 C.F.R. § 54.504(e)(2) ("An ineligible component is 'ancillary' if a price for the ineligible component cannot be determined separately and independently from the price of the eligible components, and the specific package remains the most cost-effective means of receiving the eligible services, without regard to the value of the ineligible functionality.").

subscribers or segment of the public.”¹⁴ While Jive agrees that an offer that is available generally to every member of the public would qualify, the *Clarification Order* establishes that offers to narrower classes of customers may do so as well.

Finally, with respect to the fourth criterion – “no packages of equivalent eligible services, without bundled end-user equipment, at a lower price” – Jive generally agrees with this concept, but would urge the Commission to make clear that it applies only across similarly situated customers. In Jive’s experience, for example, it is entirely possible that a customer purchasing a 10,000-line package may very well be paying a lower price, with or without phones, from one purchasing 50 lines. These variations have nothing to do with free equipment, but stem from well-recognized principles of cost causation, such as the relative economies of scale that service providers can bring to bear in serving larger volume customers, the complexity of the engagement, the level of competitive price pressure present in individual geographic markets, and other factors.

¹⁴ *Clarification Order* at ¶ 11.

Conclusion

For the foregoing reasons, Jive urges the Commission to amend the ESL to implement the Commission's recent refinements to its cost allocation policy, as described more fully herein.

Respectfully submitted,

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