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COMDTINST 5700.10A

COMMANDANT INSTRUCTION 5700.10A

16 JUNE 2008

Subj: COAST GUARD INTERNAL CONTROL PROGRAM

- Ref:
- (a) Federal Managers' Financial Integrity Act (FMFIA) of 1982, 31 U.S.C. § 3512, (P.L.97-255)
 - (b) Office of Management and Budget (OMB) Circular A-123, Management's Responsibility for Internal Control, revised December 21, 2004
 - (c) Federal Financial Management Improvement Act (FFMIA) of 1996 (P.L. 104-208)
 - (d) Office of Management and Budget (OMB) Circular A-127, Financial Management Systems, revised July 23, 1993
 - (e) Department of Homeland Security Financial Accountability Act, P. L. 108-330, October 16, 2004
 - (f) CG-00 memo dated 29 Nov 06; Decision Memo – Strategic Alternatives for Financial Management Transformation
 - (g) Reports Consolidation Act of 2000

1. **PURPOSE.** This Instruction provides guidance and information related to meeting the requirements of the Federal Managers' Financial Integrity Act (FMFIA) as interpreted by Office of Management and Budget (OMB) Circular A-123, revised. The content of this Instruction is intended to direct Coast Guard managers regarding their responsibility to establish, maintain, review, and improve internal controls through active involvement in annual assessments that support the Commandant's Annual Assurance Statements in areas noted below.

- a. Internal Controls Over Financial Reporting (ICOFR) – A statement of reasonable assurance with respect to the effectiveness of internal controls for financial reporting reliability and compliance with applicable financial laws and regulations. This assurance requires an assessment of the effectiveness of key controls in each of the ICOFR Key Process areas shown in enclosure (1).

DISTRIBUTION – SDL No.149

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NON-STANDARD DISTRIBUTION:

- b. FMFIA Section 2 – A statement of reasonable assurance with respect to the effectiveness of internal controls for program operations. This assurance requires an assessment of internal controls related to program effectiveness and efficiency and compliance with applicable laws and regulations.
- c. FMFIA Section 4 – A statement of reasonable assurance with respect to compliance with federal requirements over financial and mixed systems. This assurance requires an assessment of the level of compliance with specific financial management system requirements identified in references (c) and (d).
- d. Reports Consolidation Act – A statement of reasonable assurance with respect to the reliability of performance information reported for inclusion in the Department of Homeland Security’s (DHS) annual Performance and Accountability Report (PAR) as noted in reference (g). This assurance requires an assessment of the processes by which the Coast Guard reports performance and mission cost information in the PAR.

Each of these assessments will include an identification of Material Weaknesses and other Reportable Conditions or non-conformances to be included in the Coast Guard’s annual assurance statement to the DHS. Further definition of these conditions is provided in enclosure (3).

- 2. **ACTION.** Area, district, and sector commanders, commanders of maintenance and logistics commands, Commander Deployable Operations Group, commanding officers of Headquarters units, assistant commandants for directorates, Judge Advocate General, and special staff offices at Headquarters shall ensure that the provisions of this Instruction are followed. Internet release is authorized.
- 3. **DIRECTIVES AFFECTED.** Coast Guard Internal Control Program, COMDTINST 5700.10, dated December 15, 2005, is cancelled.
- 4. **BACKGROUND.** Internal controls can be viewed as all the methods that an organization employs to govern its activities and accomplish its purpose. The OMB defines controls as the organization, policy, and procedures that help program and financial managers achieve results and safeguard the integrity of their programs. The OMB further states that effective internal control is a key factor in achieving agency mission and program results through improved accountability, and that taking related corrective actions are critically important to creating and maintaining a strong internal control infrastructure that supports achievement of agency objectives. The assessment processes outlined below reflect a methodology that is consistent with OMB and DHS guidance in this respect.
 - a. The FMFIA of 1982 requires the head of each agency to conduct an annual evaluation of its internal controls (FMFIA Section 2) and financial management systems (FMFIA Section 4). OMB subsequently published Circular A-123 to enumerate the expectations of agencies with respect to these evaluations, and revised the circular in 2004 to require a separate focused evaluation of ICOFR. The DHS Accountability Act of 2004 reinforces the requirement for strong internal control by mandating a DHS management statement on internal control and

an independent audit of that statement beginning in fiscal year 2006. Additionally, the Reports Consolidation Act requires an assessment of performance information reported in the PAR. In turn, the Coast Guard is required to conduct assessments as a DHS component and provide annual assurances to the DHS in the areas described above.

b. These assessments will comprise a fundamental element of the Coast Guard's risk management efforts and should be viewed as manager's front line of management activity geared towards managing risk in specific areas. Internal controls are fundamentally a means of managing risk, and specifically with respect to the three internal control objectives:

- (1) Operational Effectiveness and Efficiency,
- (2) Financial Reporting Reliability, and
- (3) Compliance with Applicable Laws and Regulations.

Additionally, assessments conducted to support internal control assurance statements will be risk-based, which is to say the focus of internal controls documentation and testing will be in areas determined to present the highest risk to the organization.

5. POLICY. The internal control assessments described in further detail below will guide managers' activities related to identifying, assessing and managing risk in a specific methodical manner. These assessments will also guide managers in identifying required remediation of key internal control deficiencies and should be viewed as a means of driving continuous improvement. The Internal Control Assurance Division (ICAD), Commandant (CG-851), will be responsible for developing and communicating specific guidance consistent with this Instruction and relevant DHS directives.

a. Governance.

- (1) The governance structure for the internal control program will include a Senior Management Council (SMC), a Senior Assessment Team (SAT), responsible parties in relevant organizational segments for each assurance area (Assessable Unit Managers), and the ICAD. The SMC will serve as the senior executive body guiding the Coast Guard internal control program and related remediation efforts and making annual assurance statement recommendations to the Commandant. In that role, they will be the approving body for key decisions throughout the annual evaluation processes and will be responsible for resolving cross-directorate issues. The SAT will serve as the advisory board and primary conduit to the SMC, and will work directly with managers and the ICAD to manage and execute activities as defined in relevant procedural guidance. The responsibilities and membership of the SMC and SAT are enumerated in approved charters.

- (2) Responsible parties for each of the assurance areas are reflected in enclosures (1) and (2). For ICOFR these responsible parties are referred to as Key Process Owners, and they will have responsibility for coordinating remediation and internal control assessment activities, as well as providing an ICOFR assurance statement as it relates to financial statement assertions for their assigned key processes throughout the organization. Responsible parties for FMFIA Section 2 will have similar responsibility related to controls over their individual program operations, and Section 4 responsible parties will have similar duties related to the compliance of financial and mixed systems throughout the organization.
 - (3) The duties of Reports Consolidation Act responsible parties will similarly address assessing internal controls related to relevant mission performance information throughout the organization. Managers over these organization segments will be responsible for carrying out assessment activities to include: internal control documentation, remediation, testing, evaluation and continuous monitoring of controls. In many areas, with the exception of FMFIA Section 2 assignments, the related processes or areas of responsibility extend beyond the responsible party's organizational position or direct chain of command. To the extent internal control assessment ownership extends beyond direct reporting lines, responsible parties will be expected to conduct coordination across the organization as necessary. The Coast Guard Chief Financial Officer (CFO) will further identify the specific duties of these responsible parties and communicate them via separate correspondence.
 - (4) The ICAD will be responsible for maintaining relevant policy and procedural guidance, maintaining open communications with relevant DHS offices, and coordinating program activities through active and ongoing engagement of the SAT and Coast Guard managers. The ICAD will also serve as a source of organizational subject matter expertise and will assist Coast Guard managers through training and assistance. Additionally, they will directly coordinate the completion of program level work products defined in procedural guidance and will provide quality reviews of work products submitted by Coast Guard managers. The ICAD will facilitate communications among elements of the program governance structure and publish an annual schedule of program activities.
- b. ICOFR Assurance. The annual assessment related to the ICOFR assurance statement will follow OMB Circular A-123 (Appendix A), DHS guidance, and relevant guidance provided by Commandant (CG-851). This assessment will include an evaluation of Entity Level Controls for the organization to address the following control standards:
- (1) Control Environment – basic organizational characteristics are present and reinforced to support effective internal controls;
 - (2) Risk Assessment – processes are in place to identify external and internal risks and actively mitigate those risks;

- (3) Monitoring – ongoing monitoring is present to ensure the effective operation of controls; and
- (4) Information & Communications – processes are in place to provide for the timely and effective sharing of information throughout the organization.

The ICOFR assessment will also include an evaluation of process and transaction level controls that relate to relevant business processes. The Control Activities standard will be applied primarily in the context of the process level assessments. Assessment of process level controls will include manual controls and application controls, where application controls address specific information processing objectives for relevant information technology applications. The key elements of the process level assessment include:

- (1) Identification of significant (material) financial statement line items and the business process(es) that drive those line items;
 - (2) Identification of processes and locations subject to testing to form the basis of reasonable assurance for ICOFR;
 - (3) Documentation of processes to include identification of key controls related to relevant financial statement assertions and information processing objectives (application controls), and an assessment of the extent to which those controls are adequately designed;
 - (4) Remediation of key control design deficiencies (and control effectiveness deficiencies after testing);
 - (5) Testing of key controls to provide the documentary evidence of their effectiveness;
 - (6) Evaluation of the results of design assessments and tests of effectiveness to identify relevant deficiencies, reportable conditions and material weaknesses; and
 - (7) Reasonable assurance of compliance with applicable financial laws and regulations.
- c. FMFIA Section 2 Assurance. The OMB Circular A-123 requires a documented assessment to support a statement of reasonable assurance with respect to the following internal control objectives as they relate to program management:
- (1) Operational effectiveness and efficiency – the extent to which controls are in place and operating effectively to provide reasonable assurance that management programs are achieving stated objectives and that resources are being applied in an effective and efficient manner.

- (2) Compliance with applicable laws – the extent to which controls are in place and operating effectively to provide reasonable assurance that management programs are complying with laws and regulations that pertain to their respective areas.

Additionally, OMB Circular A-123 discusses the need to have controls in place to ensure management objectives are achieved. In view of this key point, and in the context of the standards and objectives for internal controls discussed above, the Coast Guard's assessment with respect to Section 2 will include the following characteristics:

- (1) It will address the stated internal control objectives throughout the organization. The assessment will be applied first at the Headquarters directorate level and will be expanded as appropriate to lower levels of the organization.
 - (2) Specific assessments will be conducted for each Coast Guard statutory mission program, in addition to Headquarters directorate assessments.
 - (3) The assessment will be coordinated with Office of Budget and Programs External Coordination, Commandant (CG-823), to include a review of external reports and audit findings, and determinations as to their respective resolution and potential impact on program effectiveness and efficiency.
 - (4) The assessment will be coordinated with the Office of Performance Management and Decision Support, Commandant (CG-0931), to leverage available risk assessment and performance management processes. This coordination will be conducted with the goal of moving the FMFIA Section 2 assurance process to a more highly quantitative assessment, relying on verifiable performance and cost data where possible.
 - (5) The portion of the assessment related to compliance with applicable laws and regulations will be coordinated with the Office of the Judge Advocate General (JAG) in order to provide the JAG with an opportunity to review program level evaluations.
 - (6) Coast Guard managers will use the assessment process to embed the internal control standards and related specific control activities into their management practices. This assessment must include documentation, testing, remediation, evaluation and reporting to conceptually mirror the ICOFR assessment process.
- d. FMFIA Section 4 Assurance. The FMFIA Section 4, as described in OMB Circular A-123 involves providing reasonable assurance with respect to meeting the information system requirements described in references (c) and (d). These requirements can be broken into two general categories – General Computer Controls and other Financial Management System Requirements (those enumerated in OMB Circular A-127).

- (1) General Computer Controls (GCCs) refer to controls over the information systems environment in the context of the domains identified in the Federal Information System Control Audit Manual (FISCAM). The responsible party for General Computer Controls will conduct a documented assessment of controls in each of the FISCAM domains for all financial and mixed systems as defined in reference (d) and as determined by the Coast Guard CFO. The GCCs are distinguished from Application Controls, in that Application Controls address specific process level information processing objectives and support specific financial statement assertion in the context of the ICOFR Key Process assessments, whereas GCCs apply more broadly to all financial and mixed systems. The assessment for General Computer Controls must include documentation, remediation, testing, evaluation, and reporting to conceptually mirror the ICOFR assessment process.
 - (2) Financial Management System requirements include requirements related to Generally Accepted Accounting Principles (GAAP) and the requirements of the United States Standard General Ledger (USSGL). The responsible party for these requirements will conduct documented assessments supporting an assurance that these requirements are met by all existing and new financial and mixed systems at the transaction level. These assessments will necessarily involve close coordination with the Coast Guard CIO organization.
- e. Reports Consolidation Act Assurance. The Reports Consolidation Act requires federal agencies to conduct an assessment of the completeness and reliability of the performance and financial data used in the annual PAR. In support of this assessment, the Coast Guard is required to provide assurance with respect to the performance information we submit to the DHS for inclusion in the PAR. The Program Assessment Rating Tool (PART) reports submitted to and evaluated by the Office of Management and Budget form the principle basis for this assurance. An additional basis for our assurance in this area will be the assessment of controls in the area of Mission Cost Allocation, which is the process of how we allocate expended appropriations to our statutory mission programs and the related operational data inputs. The assessment specific to the Mission Cost Allocation process will closely mirror the ICOFR assessment described above.
- f. Aggregate Evaluation and Reporting. An aggregate evaluation will be conducted for each assurance area to determine whether material weaknesses, reportable conditions, or IT system non-conformance conditions exist and the corresponding level of assurance to be reported for that area. The basis for these aggregate evaluations will be the results of internal control design assessments and testing. These evaluations will be coordinated with the SAT and SMC and assurance reporting will be drafted consistent with DHS guidelines for Commandant (CG-00) review and approval.

6. DISCUSSION. This document is intended to provide an overview of the Coast Guard's internal control assessment processes which support required annual assurance reporting to the DHS. It identifies principal responsible parties and outlines their roles and responsibilities for each of the required assurance areas. Additional detailed guidance will be promulgated separately and coordinated with the noted responsible parties.
7. DEFINITIONS. See enclosure (3).
8. ENVIRONMENTAL ASPECT AND IMPACT CONSIDERATIONS. Environmental considerations were examined in the development of this Instruction and have been determined not to be applicable.
9. FORMS/REPORTS. None.

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Assistant Commandant for Resources

Encl: (1) USCG Key Processes for ICOFR (Responsible Parties)
(2) FMFIA Section 2, Section 4 and RCA Responsible Parties
(3) Definitions

USCG Key Processes for ICOFR (Responsible Parties)

The following table reflects segmentation of financial management activity in terms of organization-wide processes that drive financial statement activity.

DHS Reference	Coast Guard Key Process	Description	Key Process Owner
1	Entity Level Control	Entity Level Controls relate to foundational controls throughout the organization and are assessed in the context of the standards of internal control using the GAO Internal Control Management and Evaluation Tool	CG 8/8D
2	General Ledger Maintenance	Processes associated with the monthly financial close and consolidation	CG 84 / FINCEN
3	Information Systems Security	General Computer Controls for financial and mixed systems (also addressed in FMFIA Section 4)	CG 62
4	Funds Balance with Treasury	Processes associated with financial statement assertions over the FBWT account	CG 84 / FINCEN
5	Budgetary Resources Management	Processes related to the budget execution cycle	CG 83
6	National Response Plan	Processes associated with the management of NRP Mission Assignments and related Accounts Receivable	CG 84
7a	Property Management – OM&S and Real Property	Financial transaction processes related to OM&S and Real Property	CG 4
7b	Property Management - Personal Property and CIP	Financial transaction processes related to Personal Property and Construction-in-Process	CG 84
9	Payment Management	Processes related to the procure-to-pay cycle, including transaction activity for relevant Doc Types	CG 84 / FINCEN
11	Revenue	Process related to revenue recognition	CG 84
12	Receivables Management	Processes related to the accounts receivable function to include orders and reimbursable agreements, billing and collections for relevant revenue sources	CG 84
13	Human Resources & Payroll	Financial transaction processes related to Human Resource and Payroll processes, to include Actuarial Liabilities	CG 1
n/a	Risk Mgt - Legal Liabilities	Process related to identifying and accounting for contingent legal liabilities	CG 094
n/a	Risk Mgt - Environmental Liabilities	Process related to identifying and accounting for contingent environmental liabilities	CG 4

FMFIA Section 2, Section 4 and RCA Responsible Parties

The following lists reflect segmentation of the organization for the purposes of noted assurance areas.

FMFIA Section 2

- CG-1, assurance with respect to program operations;
- CG-2, assurance with respect to program operations;
- CG-ACO, assurance with respect to program operations and separately for effectiveness and efficiency of statutory mission programs;
- CG-4, assurance with respect to program operations;
- CG-6, assurance with respect to program operations;
- CG-8, assurance with respect to program operations;
- CG-9, assurance with respect to program operations; and
- CG-094, assurance with respect to program operations .

FMFIA Section 4

Assurance Area	Description	Responsible Party
General Computer Controls	Responsibility for documented assessment of internal control effectiveness and necessary remediation for Coast Guard financial and mixed IT systems with respect to the 6 FISCAM domains, relevant NIST standards, and specified GCC (IT Security) Key Controls as defined by the Department	CG-6
FMFIA / OMB Circular A-127 Compliance	Responsibility for documented assessment of and necessary remediation for Coast Guard financial and mixed IT systems compliance with respect to the requirements of OMB Circular A-127; to include the integration of financial and mixed systems, GAAP compliance, and USSGL compliance at the transaction level	G-84

Reports Consolidation Act

Assurance Area	Description	Responsible Party
Mission Performance Information	Responsibility for documented assessment of and necessary remediation for the reliability of performance information included in the annual Performance Accountability Report submission to the Department	CG-51
Mission Cost Allocation	Responsibility for documented assessment of internal control effectiveness and necessary remediation for the process of allocating all Coast Guard expenditures to our statutory mission programs; to include operational and financial data inputs, subsequent allocation methods and tools, and process outputs.	TBD

DEFINITIONS

Definitions from OMB Circular A-123 (Revised):

The following definitions relate to Agency responsibilities as discussed in OMB Circular A-123 (Revised), Management's Responsibility for Internal Control. Language associated with reporting deficiencies outside the organization or agency relates to DHS reporting. Deficiencies at the component level may be reportable to the Department even if they do not represent material risks at the component level. This more stringent reporting threshold at the component level ensures that material deficiencies will not go undetected when aggregated at the agency level. In general, component level deficiencies will be reported to the Department if they are deemed to elevate to either the level of "Reportable Condition" or "Material Weakness" at the component level.

Statement of Assurance: The statement of assurance represents the agency head's informed judgment as to the overall adequacy and effectiveness of internal control within the agency. The statement must take one of the following forms:

- **Unqualified** statement of assurance (no material weaknesses reported);
- **Qualified** statement of assurance, considering the exceptions explicitly noted (one or more material weaknesses reported); or
- **Statement of no assurance** (no processes in place or pervasive material weaknesses).

Control Deficiency (*Section 2 & ICOFR*): Control deficiencies exist when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. Control deficiencies are internal to the organization and not reported externally. However, progress against corrective action plans should be periodically assessed and reported to agency management.

- **Design deficiency** - exists when a control necessary to meet the control objective is missing or an existing control is not properly designed, so that even if the control operates as designed the control objective is not always met.
- **Operation deficiency** - exists when a properly designed control does not operate as designed or when the person performing the control is not qualified or properly skilled to perform the control effectively.

Significant Deficiency (*Section 2 & ICOFR*): A deficiency in internal control, or combination of deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report data reliably in accordance with the applicable criteria or framework such that there is more than a remote likelihood that a misstatement of the subject matter that is more than inconsequential will not be prevented or detected.

Reportable Condition (*Section 2 & ICOFR*):

- **FMFIA overall** – A control deficiency, or combination of control deficiencies, that in management’s judgment, should be communicated because they represent significant weaknesses in the design or operation of internal control that could adversely affect the organization’s ability to meet its internal control objectives.
- **Financial reporting** - A control deficiency, or combination of control deficiencies, that adversely affects the entity’s ability to initiate, authorize, record, process, or report external financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity’s financial statements, or other significant financial reports, that is *more than inconsequential* will not be prevented or detected.

Reportable conditions are internal to the organization and not reported externally. However, progress against corrective action plans should be periodically assessed and reported to agency management.

Material Weakness (Section 2 & ICOFR):

- **FMFIA overall** - Reportable conditions in which the agency head determines to be significant enough to report outside of the agency.
- **Financial reporting** - Reportable condition, or combination of reportable conditions, that results in more than a remote likelihood that a *material* misstatement of the financial statements, or other significant financial reports, will not be prevented or detected.

Material weaknesses and a summary of corrective actions shall be reported to OMB and Congress through the PAR. Progress against corrective action plans should be periodically assessed and reported to agency management.

Non-conformance (Section 4): Instances in which financial management systems do not substantially conform to financial systems requirements. Financial management systems include both financial and financially-related (or mixed) systems.

Non-conformances and a summary of corrective actions to bring systems into conformance shall be reported to OMB and Congress through the PAR. Progress against corrective action plans should be periodically assessed and reported to agency management.

Definitions for FMFIA Section 2 from DHS guidance:

FMFIA Section 2 Statements of Assurance:

- Unqualified statement of assurance (no material weaknesses reported);
- Qualified statement of assurance, considering the exceptions explicitly noted (one or more material weaknesses noted); or
- Statement of no assurance (No process in place or pervasive material weaknesses); and a description of each material weakness identified.

FMFIA Section 2 Material Weakness Definition:

Material Weaknesses include reportable conditions in which the Component Head determines to be significant enough to report outside of the Component. To make this determination Component Heads should determine if a material weakness condition satisfies one or more of the following criteria:

- Merits the attention of the Executive Office of the President and the relevant Congressional oversight committees;
- Violates statutory or regulatory requirements;
- Impair fulfillment of essential operations or mission; and
- Deprives the public of needed services.