press release

PUERTO RICO FISCAL AGENCY AND FINANCIAL ADVISORY AUTHORITY

June 23, 2024

Puerto Rico Government acquires new parametric insurance to optimize coverage and payment mechanisms in response to emergencies

The new parametric insurance structure, in compliance with FEMA requirements, will facilitate and expedite payments for damage caused by natural disasters and increase coverage on the island, including Vieques and Culebra

[SAN JUAN, PR] - The Government of Puerto Rico, through the Puerto Rico Financial Advisory Authority and Fiscal Agency (AAFAF, in Spanish) and the Treasury Department, completed last Thursday, June 20, the contracting of a parametric insurance coverage, in compliance with the Federal Emergency Management Agency (FEMA) requirement known as “Obtain and Maintain” (O&M), announced AAFAF Executive Director Omar J. Marrero.

The new coverage allows the implementation of innovative instruments to access alternate capital at terms that are better than those of the traditional insurance and reinsurance markets, while also extending the coverage parameters to include the island municipalities of Vieques and Culebra, added the Secretary of State.

Last year, the Government acquired a similar parametric insurance policy, which seeks to provide coverage against specific defined events, such as hurricanes or earthquakes, by paying a fixed amount determined by the event’s magnitude upon meeting the parameters established in the policy. This is different from a traditional indemnity policy, with payments based on the magnitude of losses, requiring an adjustment process with the insurer and usually resulting in a longer period to obtain payments and forcing the Government to make advances that may affect its liquidity.

“This allows the Government to have additional liquidity to react to emergencies immediately and mitigates the risk of entering into lengthy processes with traditional insurers, which on many occasions end in litigation,” Marrero emphasized. “In addition to continuing with the parametric insurance mechanism that we began last year, we’ve implemented innovative methods using instruments available in the capital markets, accessing alternative capital that allowed us to increase the coverage for Puerto Rico and optimizing the available budget,” he added.

Meanwhile, the Treasury Department acting secretary, Nelson J. Pérez Méndez, said: “We are very pleased with the process that has been carried out, which has resulted in better coverage for the Government of Puerto Rico. The completion of this process is another big step in ensuring that Puerto Rico is ready and has the necessary resources available to deal with an emergency.”

Meanwhile, AAFAF's Deputy Executive Director and Chief Financial Officer, CPA Luis J. Umpierre, explained that, unlike the previous policy financed solely through traditional reinsurance markets, the new policy adopts a “hybrid” approach, in which a portion is financed with a Catastrophe Bond (or “Cat Bond”) issued in the capital markets without the need to record Puerto Rico's credit.

“For the past fiscal year, total coverage purchased through the traditional reinsurance markets was $220 million,” Umpierre said. “This year, a portion of the capacity funded by traditional reinsurance markets was incorporated, like last year, along with a portion of the capacity funded by the capital markets through a Catastrophe Bond. This program resulted in total coverage of over $282 million, exceeding last year's coverage by more than $60 million with virtually the same budget as last year,” the deputy executive director noted.

Through this effort, in addition to the $1.3 billion emergency reserve, the Government now has an additional layer of coverage with which, in the event of a natural disaster that meets the established parameters, it would receive immediate payment, Marrero said. “In addition, with the entry of the Government of Puerto Rico into this innovative Catastrophe Bond market, the door is opened to this new market of insurance and capital providers, increasing the menu of options for Puerto Rico in the future," he concluded.

The policy financed by the Cat Bond has a three-year term, ensuring coverage until May 31, 2027. On the other hand, the policy purchased through the traditional reinsurance markets has a term until May 31, 2025. To ensure compliance with FEMA requirements, the Government must continue to renew this type of coverage.

Meanwhile, under the O&M requirement, subrecipients - meaning municipalities, agencies, public corporations and nonprofit entities under the Public Assistance Program - must obtain and maintain insurance that is at least equal to the amount of eligible damage for the specified peril on the premises receiving assistance. Should the subrecipient fail to meet this requirement, FEMA may deny or un-allocate Federal assistance in the current disaster and deny future assistance for the facility. This applies to any permanent property receiving more than $5,000 in FEMA assistance.

###

CONTACT: Dennis Costa · 787.310.0205
dennis.costa@aafaf.pr.gov · www.aafaf.pr.gov