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Abstract

We combine two modifications to the standard (current and total income) collateral constraint that has been commonly used in models that analyze financial crisis interventions. Specifically, we consider an alternative constraint stated in terms of future and disposable income. We find that in this case a state-contingent debt tax (effective during crisis only, as opposed to a macroprudential tax) increases debt capacity and lowers the probability of crisis. This shows one more instance to call the attention of academics and policymakers to the fact that the specific form of the borrowing constraint is crucial in determining the appropriate crisis intervention.