Merit goods:

The concept of a **merit good** introduced in economics by Richard Musgrave (1957, 1959) is a commodity which is judged that an individual or society should have on the basis of some concept of need, rather than ability and willingness to pay. The term is, perhaps, less often used today than it was in the 1960s to 1980s but the concept still lies behind many economic actions by governments which are not performed specifically for financial reasons or by supporting incomes (eg via tax rebates). Examples include the provision of food stamps to support nutrition, the delivery of health services to improve quality of life and reduce morbidity, subsidized housing and arguably education.

In many cases, merit goods provide services which it is argued should apply universally to everyone in a particular situation, a view that is close to the concept of primary goods found in work by philosopher John Rawls or discussions about social inclusion. On the 'supply' side, it is sometimes suggested that there will be more support in society for implicit redistribution via the provision of certain kinds of goods and services, rather than explicit redistribution through income. Alternatively, it is sometimes suggested that society in general may be in a better position to determine what individuals need (such arguments are often criticised for being paternalistic, often by those who would like to reduce to a minimum economic activity by government).

Other possible rationales for treating some commodities as merit (or demerit) goods include public-goods aspects of a commodity, imposing community standards (prostitution, drugs, etc.), immaturity or incapacity, and addiction. A common element of all of these is recommending for or against some goods on a basis other than consumer choice. However, there is no reason why governments should not consult their populations on such issues as they increasingly do in a number of economic contexts (e.g., development planning by the World Bank or resource allocation in health systems using information on health-benefits).

In the case of education, it can be argued that those lacking education are incapable of making an informed choice about the benefits of education, which would warrant compulsion (Musgrave, 1959, 14). In this case, the *implementation* of consumer sovereignty is the motivation, rather than rejection of consumer sovereignty.

Public Choice Theory suggests that good government policies are an under-supplied merit good in a democracy.

A merit good can be defined as a good which would be under-consumed (and under-produced) in the free market economy. This is due to two main reasons:

1. When consumed, a merit good creates positive externalities (an externality being a third party/spill-over effect which arises from the consumption or production of the good/service). This means that there is a divergence between private benefit and public benefit when a merit good is consumed (ie. the public benefit is greater than the private benefit). However, as consumers only take into account private benefits when consuming merit goods, it means that they are under-consumed (and so under-produced).
2. Individuals are myopic, they are short-term utility maximisers and so do not take into account the long term benefits of consuming a merit good and so they are under-consumed

Demerit Good:

In economics, a **demerit good** is a good or service whose consumption is considered unhealthy, degrading, or otherwise socially undesirable due to the perceived negative effects on the consumers themselves. It is over-consumed if left to market forces. Examples of demerit goods include tobacco, alcoholic beverages, recreational drugs, gambling, junk food and prostitution. Because of the nature of these goods, governments often levy taxes on these goods (specifically, sin taxes), in some cases regulating or banning consumption or advertisement of these goods.

There is an important conceptual distinction between a demerit good and a negative externality. A negative externality occurs when the consumption of a good has measurable negative consequences on others who do not consume the good themselves. Pollution (due, for example, to automobile use) is the canonical example of a negative externality. Another example is cigarettes. It not only affects you, but the people around you (second hand smoking). By contrast, a demerit good is viewed as undesirable because its consumption has negative effects upon **the consumer** him/herself.

Two fundamental views in welfare economics, welfarism and paternalism, differ in their conceptual treatment of 'demerit goods'. Simply, welfarism takes the individual's *own* perception of the utility of a good as the final judgement of the utility of the good for that person, and thereby disallows the concept of a 'demerit good' (while allowing the analysis of negative externalities). As an extreme example, if a heroin addict purchases heroin, they must have done so because heroin makes them better off, and this transaction is viewed as a net social positive (assuming that the addict does not commit any other crimes as the result of their addiction).

Club goods:

Such club theory (Buchanan's Model 1965) usually concerns a cooperative, a club in which each member (rather than share of stock) has one vote and whose property is commonly owned by the membership. In Buchnan's model, the utility an individual obtains from using a club good is a function of the good as well as of the number of members in the club. Since in Buchanan's model the cost of the good is divided among the members as an equal per capita fee, the cost of the good to a member decreases with increasing club size, while congestion cost increases. The optimal size occurs where the marginal costs are equal.