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# **BUILDING AND DEMONSTRATING ENDURING VALUE**

*When Selling Your Canadian Business*

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A Comprehensive White Paper on the Frameworks,  
Metrics and Strategies That Sophisticated Buyers Evaluate

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## Executive Summary

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Canadian business owners preparing to sell face a landscape that has fundamentally changed. The certainties that underpinned decades of cross-border trade have given way to tariffs, retaliatory measures and ongoing negotiations. Interest rates, while lower than their recent peaks, remain elevated by historical standards. And the tax environment, though more favourable than initially proposed, continues to evolve.

For owners of businesses in the \$5 million to \$50 million revenue range — the lower middle market that forms the backbone of the Canadian economy — these external forces are not abstract policy debates. They directly affect valuations, buyer appetite and the strategic decisions that will determine whether an exit succeeds or fails.

This white paper provides a comprehensive framework for understanding what sophisticated buyers evaluate when assessing acquisition targets. The analytical frameworks used by institutional investors — from pension funds like CPP Investments and Ontario Teachers' Pension Plan to private equity firms and strategic acquirers — have cascaded down to inform buyer expectations across all market segments.

The message from these sophisticated buyers is clear: in an uncertain external environment, resilience has become as valuable as growth. Demonstrating that your business can withstand — and even thrive amid — tariff disruptions, economic volatility and regulatory change is now essential to commanding a premium valuation.

This white paper examines six interconnected dimensions of enduring business value:

- **The New External Environment** — Trade policy, tariffs, macroeconomic forces, tax policy and regulatory evolution reshaping Canadian business valuations.
- **Business Quality Fundamentals** — Competitive moats, pricing power and mission-critical positioning that protect cash flows from disruption and competitive attack.
- **Capital Efficiency and Financial Quality** — Return on invested capital, free cash flow conversion, capital allocation discipline and unit economics that reveal true economic value creation.
- **People, Governance and Alignment** — Management team quality, owner dependency reduction, organizational depth and incentive structures that determine whether value endures through ownership transition.
- **Risk Management and Strategic Optionality** — Concentration risk, operational resilience, scenario planning and the strategic options that create upside potential beyond the base case.
- **Integration and Execution** — Building your value story, the multi-year exit preparation timeline, navigating the transaction process and securing your legacy.

Together, these dimensions provide a roadmap for Canadian business owners who seek to maximize value and secure their legacy through a well-prepared exit.

# 1. The New External Environment

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## *Trade, Tariffs and Macro Forces Reshaping Canadian Business Value*

### 1.1 Trade Policy Disruption: A New Era of Uncertainty

The Canada-U.S. trade relationship, long described as the world's most comprehensive bilateral economic partnership, entered uncharted territory in 2025. What began in February with sweeping tariff announcements has evolved into an ongoing negotiation that continues to create uncertainty for businesses on both sides of the border.

#### The Current Tariff Landscape

As of January 2026, the tariff situation reflects a complex patchwork of measures, exemptions and ongoing negotiations. For most Canadian goods, the picture has improved significantly since the spring of 2025. Following intensive negotiations, Canada and the United States reached an understanding that allows most Canadian goods to enter the U.S. tariff-free under the Canada-United States-Mexico Agreement. According to the Royal Bank of Canada, approximately 95 per cent of non-energy Canadian exports and 100 per cent of energy exports were CUSMA-compliant by August 2025, effectively avoiding the broad-based tariffs that initially threatened to disrupt trade across virtually every sector.

However, significant tariffs remain in place for key industrial sectors. Steel and aluminium products face a 50 per cent tariff under Section 232 of the U.S. Trade Expansion Act, a rate that was increased from 25 per cent in June 2025. Copper products are subject to the same 50 per cent rate. Automobiles and certain auto parts face a 25 per cent tariff, with no CUSMA exemption. These sectoral tariffs have forced Canadian manufacturers in affected industries to fundamentally reassess their cost structures, supply chains and competitive positioning.

Canada has responded with counter-tariffs on U.S. steel, aluminium and auto imports, maintaining a 25 per cent rate on these products. The federal government removed most other retaliatory tariffs effective September 1, 2025, in recognition of the U.S. approach to CUSMA-compliant goods.

#### Implications for Business Owners

For business owners preparing for exit, the tariff environment creates both direct and indirect implications that buyers will scrutinize carefully during due diligence.

**Cross-border revenue exposure** is now a standard element of buyer analysis. Acquirers will want to understand what percentage of revenue comes from U.S. customers, whether those sales involve tariff-affected products, and what ability to pass through tariff costs has been demonstrated.

**Supply chain vulnerability** has become equally important. Even if products are not directly subject to tariffs, input costs may have increased for businesses relying on U.S. suppliers for components or materials.

**CUSMA compliance** is no longer a technical matter to be handled by customs brokers. It is a strategic asset. Businesses that can demonstrate clear CUSMA compliance — and that have the documentation to prove it — reduce buyer risk and support valuation.

## **1.2 Macroeconomic Forces: Rates, Inflation and Growth**

### **The Interest Rate Environment**

The Bank of Canada held its policy interest rate at 2.25 per cent at its January 2026 announcement, the second consecutive hold following a series of cuts that brought rates down from their 2023 peak of 5 per cent. Governor Tiff Macklem noted that while the current policy rate “remains appropriate,” heightened uncertainty makes it “difficult to predict the timing or direction of the next change.”

For business owners, the interest rate environment affects valuations in several ways. First, it influences the cost of acquisition financing. With rates now lower, financing costs have moderated, though they remain above the near-zero levels of the early 2020s. Second, interest rates affect buyer return expectations. The current rate environment represents a middle ground — not as favourable to sellers as the ultra-low-rate era, but more supportive than 2023–2024.

The Bank of Canada projects GDP growth of 1.1 per cent in 2026 and 1.5 per cent in 2027. A key source of uncertainty remains the upcoming review of CUSMA, scheduled for 2026.

### **Inflation and Input Costs**

Consumer price inflation rose to 2.4 per cent in December 2025. For business owners, the inflation environment of recent years has been a test of pricing power. Those who successfully passed through cost increases to customers without losing market share have demonstrated a valuable competitive advantage.

## **1.3 Tax Policy: Relief and Opportunity**

### **Capital Gains: The Inclusion Rate Stays at 50 Per Cent**

In one of the most significant reversals in recent tax policy, the federal government announced in March 2025 that it would cancel the proposed increase to the capital gains inclusion rate. The inclusion rate remains at 50 per cent, rather than increasing to 66.67 per cent as had been proposed in the 2024 federal budget.

### **The Lifetime Capital Gains Exemption**

The Lifetime Capital Gains Exemption for qualified small business corporation shares increased to \$1.25 million, effective June 25, 2024. This exemption allows business owners to shelter a substantial portion of their capital gains from tax entirely when selling shares of a qualifying business.

### **The Canadian Entrepreneurs' Incentive**

A new Canadian Entrepreneurs' Incentive reduces the inclusion rate to 33.33 per cent on up to \$2 million in eligible capital gains over a taxpayer's lifetime, phasing in gradually. Combined with the \$1.25 million LCGE, qualifying entrepreneurs could ultimately benefit from preferential treatment on up to \$3.25 million in capital gains.

### **Intergenerational Transfers and Employee Ownership Trusts**

Bill C-208, enacted in 2021, levelled the playing field for intergenerational transfers. Employee Ownership Trusts offer a \$10 million capital gains exemption for qualifying sales completed before December 31, 2026.

## **1.4 Regulatory Evolution and Technology Disruption**

ESG considerations have moved from the periphery to the centre of buyer due diligence. BDC research indicates that 92 per cent of major corporate buyers now require suppliers to disclose at least one ESG criterion. Privacy legislation continues to tighten, with Quebec's Law 25 now in full effect. Cybersecurity has become a material due diligence issue. And the rapid advancement of artificial intelligence presents both opportunity and threat.

## 2. Business Quality Fundamentals

### *Competitive Moats, Pricing Power and Mission-Critical Positioning*

Understanding external forces addresses only half the equation. The other half is internal: the fundamental qualities of a business that determine whether it can withstand external pressures and continue generating cash flows for its new owners.

### 2.1 The Competitive Moat

The term “economic moat” was popularized by Warren Buffett, drawing an analogy between medieval castles and businesses.

*“Every day, in countless ways, the competitive position of each of our businesses grows either weaker or stronger. If we are delighting customers, eliminating unnecessary costs and improving our products and services, we gain strength. But if we treat customers with indifference or tolerate bloat, our businesses will wither. On a daily basis, the effects of our actions are imperceptible; cumulatively, though, their consequences are enormous. When our long-term competitive position improves as a result of these almost unnoticeable actions, we describe the phenomenon as ‘widening the moat.’”*

— Warren Buffett, September 2001

### Types of Moats in the Lower Middle Market

**Switching costs** arise when customers face significant barriers to changing suppliers. **Network effects** occur when a product becomes more valuable as more people use it. **Cost advantages** derive from economies of scale, proprietary processes or geographic factors. **Intangible assets** include brand recognition, patents, regulatory licences and proprietary data. **Geographic and regulatory moats** are particularly relevant in the Canadian context — Canada’s vast geography, dispersed population and bilingual requirements create natural barriers.

### How Buyers Assess Moat Durability

*“We are trying to figure out what is keeping — why is that castle still standing? And what’s going to keep it standing or cause it not to be standing five, 10, 20 years from now. What are the key factors? And how permanent are they?”*

— Warren Buffett

### 2.2 Pricing Power: The Single Most Important Indicator

*“The single most important decision in evaluating a business is pricing power. If you’ve got the power to raise prices without losing business to a competitor, you’ve got a very good business. And if you have to have a prayer session before raising the price by 10 percent, then you’ve got a terrible business.”*

— Warren Buffett, Financial Crisis Inquiry Commission, 2010

## Evidence of Pricing Power

Demonstrating pricing power requires concrete evidence: **historical price increase track record**, **cost pass-through ability** through the tariff and inflation environment, and **contract structures** with automatic escalation clauses or cost-plus provisions.

## The Pricing Power Paradox

Businesses with the strongest pricing power may not have exercised it fully. A company that has raised prices modestly despite having the ability to charge more has untapped pricing power that represents value for a buyer.

## 2.3 Mission-Critical Positioning

The “3 a.m. phone call” test is instructive: if something goes wrong in the middle of the night, would your customer call you? Businesses that pass this test occupy a privileged position.

## Revenue Quality Hierarchy

Buyers evaluate revenue from most to least valuable:

- **Contractually recurring revenue** — subscriptions, maintenance agreements, long-term service contracts.
- **Consumable or replacement revenue** — products used up and repurchased.
- **Repeat project revenue** — project-based work with returning customers.
- **New customer project revenue** — one-time projects with new customers.

## 2.4 Intellectual Property and Organizational Capital

Beyond formal intellectual property (patents, trademarks, trade secrets, copyrights), businesses accumulate organizational capital — documented processes, proprietary data and institutional knowledge. Canadian-specific considerations include SR&ED credits, cross-border IP structures and IP as tariff insulation.

## 3. Capital Efficiency and Financial Quality

### *Return on Invested Capital, Cash Flow and Unit Economics*

For many business owners, financial analysis begins and ends with EBITDA. But sophisticated buyers look well beyond EBITDA. EBITDA measures earnings, but it does not measure value creation.

### 3.1 Return on Invested Capital: The True Measure

ROIC measures the return generated on the capital invested in the business. If returns exceed the cost of capital, the business creates value. If not, it destroys value — regardless of revenue or profit levels.

#### Why ROIC Matters More Than EBITDA

Consider two businesses, each generating \$5 million in EBITDA. Business A requires \$10 million in invested capital; Business B requires \$25 million. Business A generates a 50 per cent ROIC; Business B generates 20 per cent. Buyers will pay higher multiples for Business A.

*“Return on invested capital (ROIC) is often just as important — and occasionally even more so — as a measure of value creation and can be easier to sustain at a high level. When a company’s ROIC is already high, growth typically generates additional value. But if a company’s ROIC is low, executives can create more value by boosting ROIC than by pursuing growth.”*

— McKinsey & Company, “Balancing ROIC and Growth to Build Value”

#### Presenting ROIC Effectively

Key aspects include: **ROIC trend over time** (five to 10 years), **ROIC versus cost of capital** (the spread matters), **ROIC stability through cycles**, and **ROIC by segment** (revealing where value is created or capital misallocated).

### 3.2 Free Cash Flow Conversion and Quality

“Cash is fact, profit is opinion.” **FCF to EBITDA** measures how much EBITDA converts to free cash. **FCF to net income** should generally exceed 100 per cent over time. Buyers also assess **operating cash flow quality** and **capital intensity**, distinguishing between maintenance and growth CapEx.

### 3.3 Capital Allocation Track Record

Businesses have four fundamental options for deploying capital: reinvest in organic growth, acquire other businesses, pay down debt or return capital to owners. **Return on incremental invested capital (ROIIC)** reveals whether the business can continue creating value as it grows. **Reinvestment runway** determines how long high returns can compound.

### 3.4 Unit Economics: Proving the Engine Works

Core metrics include **gross margin by product or service line**, **customer acquisition cost (CAC)**, **customer lifetime value (LTV)**, and the **LTV-to-CAC ratio** (3:1 or higher is generally healthy). **Cohort analysis** tracks customer behaviour by acquisition date, revealing whether revenue cohorts expand or contract over time.

### **3.5 Preparing for Quality of Earnings Analysis**

Most middle-market transactions include a Quality of Earnings analysis. Common areas of focus include normalizing adjustments, working capital analysis, revenue recognition, tariff cost treatment and foreign exchange. Many sellers now commission sell-side QofE reports before going to market.

## 4. People, Governance and Alignment

### *Management Quality, Organizational Depth and Incentive Structures*

Buyers are purchasing the future. Competitive moats can erode, pricing power can weaken and financial performance can change — depending on the quality of the people who manage the business.

*“We can afford to lose money — even a lot of money. But we can’t afford to lose reputation — even a shred of reputation. We must continue to measure every act against not only what is legal but also what we would be happy to have written about on the front page of a national newspaper in an article written by an unfriendly but intelligent reporter.”*

— Warren Buffett, memo to Berkshire Hathaway managers

### 4.1 Management Team Assessment

Buyers assess: **Strategic capability** — track record, disruption response, market understanding. **Operational excellence** — consistent delivery, process maturity, continuous improvement. **Financial acumen** — capital allocation discipline, working capital management. **Leadership and people development** — team building, talent pipeline, culture. **Integrity and character** — transparency, self-awareness, reputation.

### 4.2 Owner Dependency: The Critical Risk Factor

For owner-operated businesses, owner dependency is often the single most significant risk factor. It manifests through customer relationships, supplier relationships, technical knowledge, decision authority and sales capability held personally by the owner.

#### Reducing Owner Dependency

This is a multi-year project: building management depth, delegating authority progressively, documenting processes and knowledge, transitioning relationships, and establishing a track record under reduced owner involvement — ideally 12 to 24 months before going to market.

### 4.3 Organizational Depth and Succession Planning

The “second tier” of management is critical for execution capability, succession depth, growth capacity and as a signal of leadership quality. Formal succession planning demonstrates organizational maturity and reduces transition risk.

### 4.4 Governance Structures and Internal Controls

Establishing a board of directors or advisors before going to market provides strategic input, management development, governance credibility and transaction support. Financial reporting quality, internal controls and compliance all affect valuation and transaction execution.

## **4.5 Incentive Alignment**

Incentive alignment encompasses base compensation benchmarking, short-term incentive design, long-term equity-like incentives and retention provisions. Employee ownership arrangements — including ESOPs and Employee Ownership Trusts — must be addressed in transactions.

## 5. Risk Management and Strategic Optionality

### *What Could Go Wrong, What Could Go Right, and Positioning for Multiple Futures*

Sophisticated buyers think probabilistically, asking not only “what is this business worth today?” but “what could happen that would change that value dramatically?”

*“We don’t have to be smarter than the rest. We have to be more disciplined than the rest.”*

— Warren Buffett

*“Rule No. 1: Never lose money. Rule No. 2: Never forget Rule No. 1.”*

— Warren Buffett

### 5.1 A Framework for Business Risk Assessment

**Concentration risk** — customer, supplier, product, geographic and key person concentration each create vulnerability. If a single customer represents 20 per cent or more of revenue, buyers will scrutinize that relationship intensely.

**Operational risk** — technology and systems risk, facility and equipment risk, process and quality risk, and supply chain risk.

**Financial risk** — leverage and liquidity, working capital volatility, currency and commodity exposure, interest rate sensitivity.

**Strategic and external risk** — competitive dynamics, technology disruption (particularly AI), market evolution, regulatory and policy risk, economic cycles, geopolitical risk (including the 2026 CUSMA review), and climate risk.

### 5.2 Demonstrating Resilience

The strongest evidence is historical performance through actual disruptions: the COVID-19 pandemic, supply chain disruptions, inflationary pressures and tariff disruptions. Buyers also assess **risk mitigation infrastructure** and expect **scenario planning and stress testing** for key scenarios including loss of largest customer, economic recession, tariff escalation, technology disruption and key person loss.

### 5.3 Strategic Optionality: Positioning for Upside

Options include geographic expansion, product or service extension, customer segment expansion, channel development, acquisition opportunities, pricing optimization and operational improvement. Valuable options are **credible, exclusive, economically attractive, timing flexible** and have **downside protection**.

### 5.4 Trade Policy Optionality

Trade-related options include domestic market focus, supply chain flexibility, U.S. manufacturing or operations, CUSMA optimization and market diversification leveraging CETA and CPTPP.

## **5.5 ESG Considerations**

Environmental considerations include carbon footprint, environmental compliance, climate risk and sustainability opportunities. Social considerations include workforce practices and community impact. Governance considerations are increasingly formalized into structured assessments by institutional buyers.

## 6. Integration and Execution

### *Building Your Value Story, Preparing for Transaction and Securing Your Legacy*

*“I don’t look to jump over seven-foot bars; I look around for one-foot bars that I can step over.”*

— Warren Buffett

The goal is to present a business whose quality is so evident that buyers can see it clearly — a one-foot bar they can step over with confidence.

### 6.1 Building Your Value Story

#### The Core Questions Every Buyer Asks

Every buyer seeks answers to eight fundamental questions: What does this business do, and for whom? Why does this business win? How sustainable are those advantages? What are the economics? Who runs it, and can they continue? What could go wrong? What could go right? And why now?

#### Evidence Over Assertion

The most common weakness in value stories is assertion without evidence. Instead of “we have loyal customers,” provide retention rates and relationship tenure. Instead of “we have pricing power,” provide price increase history and margin trends. Sophisticated buyers will probe every claim.

### 6.2 The Exit Preparation Timeline

The CFIB has documented that only 9 per cent of business owners have a formal succession plan. Those who begin planning early achieve better outcomes.

**Three to five years before exit:** Strategic clarity, management development, financial discipline, risk reduction and governance formalization.

**Two to three years before exit:** Performance track record under reduced owner involvement, financial statement quality, legal and compliance cleanup, data room preparation and advisor selection.

**Twelve to twenty-four months before exit:** Value story development, sell-side quality of earnings, tax planning, personal planning and market assessment.

**Six to twelve months before exit:** Go/no-go decision, marketing materials, buyer identification and management preparation.

### 6.3 Navigating the Transaction Process

The transaction process typically spans six to twelve months across six phases: market approach and initial interest, buyer evaluation and indications of interest, management presentations and diligence, letters of intent and exclusivity, confirmatory due diligence, and definitive agreements and closing.

## **6.4 Canadian-Specific Transaction Considerations**

Canadian M&A transactions involve specific considerations including asset versus share sale structure, LCGE and CEI optimization, intergenerational transfer provisions, Employee Ownership Trust rules, Investment Canada Act review (net benefit and national security), and Competition Act considerations.

## **6.5 Securing Your Legacy**

Legacy considerations often influence buyer selection beyond price — preservation of company culture, employee retention, investment in growth and maintenance of customer relationships. Planning for life after the transaction is as important as planning for the transaction itself.

## Conclusion: The Journey Ahead

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Enduring value is not created in the months before a transaction. It is built over years of strategic focus, operational discipline, team development and customer commitment. The business owners who achieve the best outcomes are those who build businesses worthy of premium valuations — not those who package mediocre businesses cleverly.

The Canadian lower middle market — businesses with \$5 million to \$50 million in annual revenue — represents a vital segment of the national economy. According to Statistics Canada, small and medium enterprises contribute 48 per cent of GDP and employ nearly two-thirds of the private sector workforce. The Canadian Federation of Independent Business estimates that 76 per cent of business owners plan to exit within the next decade, with \$2 trillion in business assets potentially changing hands.

For these business owners, the coming years will be decisive. Those who prepare thoughtfully — building value, strengthening teams, managing risks and positioning for transaction — will secure the legacies they have worked so hard to create.

The choice is yours. The time to begin is now.

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With over 30 years of business leadership experience, Karl has founded eight companies, facilitated over \$4 billion in transaction value and achieved five consecutive years on the PROFIT 500 list. He holds the ICD.D designation from the Institute of Corporate Directors, serves on not-for-profit boards, and is actively involved in the Canadian M&A ecosystem through organizations including ACG Toronto and M&A Club Canada.

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