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Risk-Based Regulation: A Case Study

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Risk-based regulation is now the norm. While there are many ways of describing it, [Julia Black, Professor of Law at the London School of Economics and Political Science](#) terms it as:

targeting regulation and regulatory effort on things which pose the greatest risks to society or to regulatory objectives.... Risk-based regulation at the operational level means targeting regulatory resources on those organizations or activities which pose the greatest risk to the regulator's objectives, which are usually legally defined.

However, implementing an effective risk-based regulatory approach is difficult. What are the best indicators that a registrant poses a risk of harm? How should those indicators be analyzed? Once analyzed, what regulatory tools are most appropriate for that particular risk? What resources should be allocated? Who should make these decisions? Who monitors and evaluates (and directs modifications to) the approach?

Some guidance might be gleaned from the sudden collapse of an association of UK law firms, known as PM Law, in February 2026. The [BBC reported](#) that over 600 staff learned they had lost their jobs from a paper notice posted on the office windows when they arrived for work. Tens of thousands of matters (including real estate transactions in the midst of closing, personal injury claims, and wills and estate matters) were interrupted. It was estimated that £39.5 million of trust funds were improperly removed or misused. The regulator, the Solicitors Regulation Authority (SRA), [made £30 million](#) in compensation payments.

The SRA retained the international law firm of Jenner & Block to provide a [Serious Event Review](#) of whether the SRA could have intervened earlier and, if so, to make recommendations for improvement. Many of the lessons from that Review can be extrapolated to other regulators' risk-based regulation approaches.

The Review found that the SRA could have identified and intervened earlier, reducing the resulting harm:

- The unconventional corporate structure of PM Law caused the SRA to not treat it as a single entity. While there were about a dozen entities, they were run on a centralized basis including IT and accounting functions. Two individuals, only one of whom was a lawyer, managed the group's compliance with its financial and legal obligations.
- "As an institution, the SRA held a substantial body of information about the PM Law Group before the intervention." This included two forensic investigations, an anti-money laundering inspection, a random compliance inspection, categorization of PM Law as adopting an aggressive growth strategy (that made it a "High Risk" entity for a period of time), and several complaints against registrants and firms within the group. However, that knowledge "was distributed across different teams, systems and individuals, and was never drawn together into a single, composite picture of the risk [that PM Law] presented." Also, "[t]hat failure of aggregation is, in our view, the central finding of this [Review]."
- Several individual concerns were closed because they were treated in isolation.
- Because there was no clear picture of the risk PM Law created, concerns were frequently not escalated, and when they were, regulatory actions were delayed and conducted with insufficient rigour. There were few failures by individual SRA staff. "What was missing was the ability to convert that engagement into timely and effective regulatory action." For example, senior management and the Board were unaware, before PM Law collapsed, of information "which

might suggest financial instability and accounting rules concerns...."

- There were instances in which the SRA investigators, inspectors, and auditors took PM Law's explanations at face value when the overall risk picture suggested that verification of data was indicated.
- Some key departments in the SRA had significant capacity concerns preventing it from allocating adequate resources to high-risk registrants.

The Review made the following recommendations for improving the SRA's risk management approach (some of which are already underway):

- The SRA "needs the technological capability to aggregate intelligence across workstreams so that decision-makers see a complete picture of an entity at the point of decision." This might include "a risk assessment matrix that would allow for quantitative assessment of the risk of each individual case."
- Some of the SRA staff need better training and supervision when doing complex regulatory work, such as forensic inspections and risk assessments.
- The SRA "needs fully defined escalation criteria so that the accumulation of very serious concerns reaches the appropriate level in the organisation without depending on the initiative of individual officers."
- These recommendations do not mean that the Board (or even the CEO) should manage individual high-risk matters. What is needed is a risk-based regulation system that provides meaningful assurance that

risks are being identified, assessed, and addressed appropriately.

Interestingly, a few days before the Review was released, Ontario developments reflected similar themes. The Real Estate Council of Ontario (RECO) has also recently faced the collapse of a large industry entity that resulted in a significant loss of trust funds. There is [a consultation proposal](#) on several suggested changes that would facilitate enhanced risk-based regulation, including:

- Creating a new category of registration for those who manage or supervise a brokerage.
- Requiring brokerages to establish policies covering the conduct of their staff and agents in high-risk situations.
- Clarifying and expanding trust account requirements.
- Requiring brokerages to submit annual financial filings with RECO and to prepare monthly trust account reconciliation statements that can be produced to RECO upon request.
- Allowing the issuance of compliance orders, which can take effect

immediately in urgent circumstances, without an application to court.

- Permitting the imposition of a freeze order (to protect monies) at a more preliminary stage than is currently authorized.
- Permitting the imposition of administrative monetary penalties for violations of regulatory requirements. The amount of the penalty would increase with the degree of risk of harm to the public from the conduct.

These proposals would provide additional useful risk indicators and permit a proportionate and timely risk-based response to concerns.

Similarly, the Law Society of Ontario has [recently implemented a requirement](#) for law firms to provide an irrevocable authorization for the Society to verify trust fund information with the law firm's financial institution. This additional measure addresses the concern about taking registrants' explanations at face value.

Risk-based regulation is becoming more sophisticated.

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