STATE OF ILLINOIS
SECRETARY OF STATE
SECURITIES DEPARTMENT

IN THE MATTER OF: GARY N. FERRARO	)	FILE NO. 0500520

ORDER OF REVOCATION

TO THE RESPONDENT: Gary N. Ferraro
(CRD#: 2470858)
222 Taylor Court
Buffalo Grove, Illinois 60089

WHEREAS, the above-captioned matter came on to be heard on January 5, 2006 pursuant to the Notice of Hearing dated November 1, 2005, FILED BY Petitioner Secretary of State, and the record of the matter under the Illinois Securities Law of 1953 [815 ILCS 5] (the "Act") has been reviewed by the Secretary of State or his duly authorized representative.

WHEREAS, the rulings of the Hearing Officer on the admission of evidence and all motions are deemed to be proper and are hereby concurred with by the Secretary of State.

WHEREAS, the proposed Findings of Fact, Conclusions of Law and Recommendations of the Hearing Officer, James L. Kopecky, Esq., in the above-captioned matter have been read and examined.

WHEREAS, the proposed Findings of Fact of the Hearing Officer are correct and are hereby adopted as the Findings of Fact of the Secretary of State:

1. The Department served Respondent with a Notice of Hearing on March 6, 2006.

2. The Respondent failed to timely answer, appear, or submit a responsive pleading.

3. The Respondent failed to appear at the time and place scheduled for hearing and failed to request a continuance.

4. That all relevant times, the Respondent was registered with the Secretary of State as a salesperson in the State of Illinois pursuant to Section 8 of the Act until February 18, 2004.

5. That on July 5, 2005, the NASD entered an Order Accepting Offer of Settlement submitted by the Respondent ("Order") regarding Disciplinary Proceeding No. EAF0300890003, which barred Respondent from association with any NASD member in all capacities.

6. That the AWC found:

    a. Between approximately November 2001 and September 2003 (the "relevant period"), the Respondent, first at McDonald and then at First Allied, facilitated the deceptive efforts of his customers to engage in market timing transactions in mutual funds that exceeded the limits of, and therefore violated, the funds' prospectuses.

    He assisted his customers in two ways. First, he negotiated or knew about and authorized quid pro quo arrangements with fund companies to enable certain of his customers (the "market timing clients") to trade mutual funds in violation of the limits established in the funds' prospectuses. Under these secret arrangements, which were not disclosed to other shareholders of the mutual funds, called "sticky asset" or "sticky money" deals, his clients made a long-term investment in one fund in an mutual fund complex (the "sticky money") for the opportunity to market time other funds in the same family up to the same amount.

    Second, the Respondent also facilitated other market timing clients' attempts to disguise their identity and avoid fund restrictions. In particular, after a mutual fund sought to restrict the clients' market timing, the clients, through the Respondent, opened other accounts which had the same beneficial owner and, through those new accounts, market timed funds in the same fund family.

    With the Respondent's assistance, his clients were able to engage in their deceptive behavior and make 117 exchanges that exceeded mutual fund prospectus limits or violated fund restrictions. The clients earned substantial illicit profits. The Respondent earned management fees from this activity totaling approximately $68,366.34. The Respondent's facilitation of his clients' activities described herein was contrary to the high standards of commercial honor and just and equitable principles of trade required by NASD Conduct Rule 2110.

b. Market Timing Mutual Funds

"Market timing" is the short term buying and selling of mutual fund shares to exploit inefficiencies in mutual fund pricing. The share price of a mutual fund is determined by the "net asset value" of the funds. The "net asset value" of mutual funds holding equities typically is calculated once per day based on the closing price of the underlying securities as of 4:00 p.m. EST. Because mutual funds typically are priced only once per day, market timers may have an opportunity to engage in arbitrage based on market information that may not be reflected in that day's net asset value. To accomplish the arbitrage, market timers typically buy and sell shares on a short-term basis, realizing quick gains and then retreating to the previous market position. Market timing may harm other mutual fund investors by raising mutual funds' transaction costs, such as taxes and trading costs, and by requiring funds to retain more assets in liquid investments with lower returns, including cash positions. For these reasons, some mutual fund complexes attempt to discourage or restrict frequent trading in certain funds through restrictive language in their prospectuses or statements of additional information, limiting shareholders to a certain number of transactions or imposing fees on redeeming fund shares after a certain number of transactions, or by seeking to limit trading that exceeds the parameters in the prospectus.

To maintain their ability to market time mutual funds, market timers have engaged in a number of deceptive practices. They entered into secret arrangements with fund advisors called sticky assets deals, which were not disclosed to other shareholders of the mutual funds. They also used multiple accounts under the same beneficial owner in such a manner that disguised their identities, thwarting mutual fund attempts to restrict or stop their market timing activity.

c. The Respondent Facilitated A Sticky Assets Deal That Enabled One of his Clients to Market Time a Mutual Fund in Violation of the Fund's Prospectus

In November 2001, the Respondent, on behalf of one of his hedge fund clients, PM, agreed to an undisclosed arrangement with IFG, the investment advisor for the Mutual Fund I funds, which permitted PM to trade in Mutual Fund I beyond the limits established in the Funds' prospectus.

Mutual Fund I represented to its investors in prospectuses that "You may make up to four exchanges out of each Fund per twelve-month period, but you may be subject to a redemption fee or front-end sales

charge described below." The Respondent knew or should have known about these restrictions.

The Respondent, on behalf of PM, accepted the terms of the sticky assets deal and PM invested $3 million in long-term assets (or "sticky assets" or "sticky money") in one of Mutual Fund I's funds. In return, IFG provided PM the opportunity to market time up to $3 million in another fund in Mutual Fund I's complex. The Respondent's involvement with this arrangement on behalf of PM began while he was employed at McDonald, and PM continued trading pursuant to such arrangement in accounts it established with the Respondent at First Allied. At no time did IFG disclose this arrangement to other investors in funds in Mutual Fund I's complex. For PM's accounts established at First Allied, IFG reduced the limit the Respondent could market time in Mutual Fund I's complex to $1.9 million.

Pursuant to the sticky assets deal with Mutual Fund 1, PM was permitted to execute up to two round trips (a round trip typically is defined as redeeming shares in fund A and purchasing shares in fund B, then redeeming shares in fund B and purchasing shares in fund A, i.e., two exchanges) a month in a fund in Mutual Fund is family. This allowed PM to exceed the four exchange out limit in Mutual Fund I's prospectus.

Between November 2001 and April 2003, through the Respondent, PM executed 68 exchanges in Mutual Fund I, well in excess of the limits established in Mutual Fund I's prospectus.

The Respondent thus substantially assisted PM to engage in excessive market timing contrary to the fund prospectus. He knew IFG did not make such trading privileges available to the general public. PM thereby profited at the expense of fund investors.

d. The Respondent Knew of and Authorized A Sticky Assets Deal to Enable Another of his Clients to Market Time in Violation of Exchange Limits

From April until July 2003, the Respondent's client CP engaged in market timing in certain mutual funds in the Mutual Fund S family pursuant to a sticky assets deal he knew about and authorized with a representative of DWS, the investment advisor for funds in the Mutual Fund S complex.

Mutual Fund S represented to its investors in prospectuses that:

Up to eight exchanges may be effected free of charge in any calendar year. Thereafter, to discourage the potential adverse impact on the Sub-Funds and their Shareholders of abuses of this exchange privilege, the Company may impose an exchange charge that currently may not exceed 50% of the net asset value of the Shares

being submitted for exchange.

The Respondent knew or should have known of the prospectuses' exchange limitations.

Pursuant to the sticky assets deal, CP was able to market time approximately $5 million in certain of Mutual Fund S funds and execute one round trip per fund per quarter, in exchange for investing $5 million in long-term ("sticky money") in another of Mutual Fund S funds. On approximately April 17, 2003, CP invested approximately $5 million in sticky money in one of the Mutual Fund S funds. Between approximately April 28 and July 14, 2003, CP engaged in market timing in three other funds in the Mutual Fund S family. In trades effected through First Allied, CP executed 17 exchanges nine more than the limits established in Mutual Fund S prospectus.

Through this deal with DWS, the Respondent substantially assisted CP to engage in excessive market timing contrary to the fund prospectus. Such trading privileges were not available to the general public. CP thereby profited at the expense of fund investors.

e. The Respondent Facilitated His Clients' Deceptive Practices Designed to Avoid Mutual Fund A's Attempts to Restrict Market Timing in its Funds

i. Activity at McDonald

The Respondent had a market timing agreement with Mutual Fund A. The agreement allowed him to make exchanges between Mutual Fund A funds for several of his clients' accounts with a single faxed instruction sheet. The market timing agreement also provided, consistent with the prospectus for Mutual Fund A:

Timers will be permitted 10 exchanges or buy/sell transactions per calendar year per (Mutual Fund A's) prospectus. An exchange is the movement out of (redemption) one fund and into (purchase) another fund. For example: An exchange from an equity fund to a money market fund is one exchange; the subsequent move to another equity fund or to the original fund, counts as the second exchange, and so forth. Once the 10-exchange limit is reached, a stop code will prevent further exchanges.

Furthermore, the Respondent knew or should have know that prospectuses for Mutual Fund A limited an investor to

ten exchanges per calendar year and that Mutual Fund A discouraged market timing activity. The prospectus stated:

You are limited to a maximum of 10 exchanges per calendar year, because excessive short term trading or market-timing activity can hurt fund performance. If you exceed that limit, or if a [Mutual Fund A] Fund or the distributor determines, in its sole discretion, that your short-term trading is excessive or that you are engaging in market timing activity, it may reject any additional exchange orders.

Between February and October 2002, the Respondent had five clients whose accounts were all managed by the same hedge fund manager. Each of these clients, with the Respondent's assistance, circumvented the 10-exchange limit set forth in the Mutual Fund A agreement and prospectuses and made in excess of 10 exchanges in Mutual Fund A's funds

Each of these clients opened an account through the Respondent with McDonald for the sole purpose of market timing funds. The Respondent knew that each client intended to specifically market time Mutual Fund A funds. After the client's account either neared or reached the 10-exchange limit, McDonald and the clients received from Mutual Fund A either a warning letter or a restriction letter, respectively. McDonald forwarded each letter to the Respondent's team. These letters each contained similar language. For example, the warning letters stated that the referenced account had made either 8 or 9 exchanges and that only 10 exchanges were permitted in a calendar year. Similarly, the restriction letter stated that the referenced account had made the allotted 10 exchanges and therefore would not be permitted to make any further exchanges for the remainder of the year. After receiving either letter, the client transferred money from that account to a newly opened account at McDonald. The Respondent remained the representative of record for each account. The client then continued market timing in Mutual Fund A funds until the new account neared or reached the 10-exchange limit, at which time the client transferred the money to another newly opened account, where the process continued. As a result, these five clients each made between 24 and 26 exchanges in Mutual Fund.

The Respondent's team received from Mutual Fund A 14 warning letters and one restriction letter regarding these accounts.

A funds during this nine-month period, each exceeded the limits established in Mutual Fund A's prospectus, and each profited from this activity.

ii. Activity at First Allied

One of the Respondent's clients, MMRW, managed several hedge funds that had the same beneficial owner. MMRW, with the Respondent's assistance, used accounts opened for these hedge funds to avoid attempts by Mutual Fund A to restrict its market timing activity by continuing to market time funds in Mutual Fund A's family after Mutual Fund A had restricted a related account. With the Respondent's assistance, MMRW therefore was able to execute market timing transactions beyond the limitations established in the prospectuses governing mutual funds in Mutual Fund A's complex.

The Respondent knew or should have known that prospectuses for Mutual Fund A limited an investor to ten exchanges per calendar year and that Mutual Fund A discouraged market timing activity.

In approximately November 2002, the Respondent opened the first of several accounts for hedge funds managed by client MMRW at First Allied; the Respondent was the representative of record for the initial and subsequent hedge fund accounts opened by MMRW. MMRW opened the first account for Hedge Fund N, a hedge fund it managed. MMRW market timed in Mutual Fund A's complex through Hedge Fund N's account. Between approximately December 30, 2002 and April 23, 2003, MMRW, in trades through First Allied, executed multiple exchanges in Hedge Fund N's account in two of Mutual Fund A's funds. On April 23, 2003, Mutual Fund A restricted trading in Hedge Fund N's account.

Mutual Fund A's April 23 letter stated:

Over the past few months, we have closely monitored the effects of market timing and short-term trading within our family of funds. We have determined that these activities, if not properly addressed, may hinder our ability to achieve

desirable long-term investment results for our shareholders; therefore we can no longer accommodate these activities. In accordance with the prospectus, all shareowners are restricted to a maximum of 10 exchanges. Additionally, if a [Mutual Fund A] Fund or the distributor determines, in its sole discretion that your short-term trading (buys and sells) is excessive, it may reject any of your purchase orders.

As of April 23, 2003, these accounts have already reached their exchange limit or have been identified as having excessive short-term trading activity for the year. Please note that these accounts have been stopped and will no longer be permitted orders in 2003.

On approximately May 23, 2003, the Respondent opened two additional accounts for MMRW for hedge funds PB and PH, which MMRW managed. The Respondent knew or should have known that Hedge Funds N, PB and PH had the same beneficial owner.

After Mutual Fund A restricted Hedge Fund N's account from market timing, MMRW closed the Hedge Fund N First Allied account on approximately June 16, 2003 and wired all assets in the account, totaling approximately $4.07 million, to a bank account it controlled. The next day, MMRW wired approximately $4.07 million from a bank account to Hedge Fund PB's First Allied account. MMRW then market timed funds in Mutual Fund A's complex through Hedge Fund PB's account.

Between June 26, 2003 and August 14, 2003, in trades executed by the Respondent's team through First Allied, Hedge Fund PB made a total of 16 exchanges in the same funds in Mutual Fund A's complex that Hedge Fund N had market timed. Mutual Fund A restricted trading in the PB account on August 14, 2003. Mutual Fund A notified the Respondent's team of the restriction by a letter containing the same language as the April 23 letter. On approximately August 26, 2003, Hedge Fund PB's account was closed, and all proceeds from the account were wired to the same bank account that Hedge Fund N had wired assets to on June 16, 2003.

MMRW thereafter commenced market timing funds in Mutual Fund A's complex through Hedge Fund PH's account. Between approximately September 2 and 10, 2003,

Hedge Fund PH invested $12 million in Mutual Fund A's cash reserve fund in four $3 million increments. On approximately September 16, 2003, Hedge Fund PH invested $3 million in two of Mutual Fund A's funds, and $4 million and $2 million in two other Mutual Fund A funds (including the same mutual funds that Hedge Funds N and PB had market timed). One day later, Hedge Fund PH redeemed each Mutual Fund A fund purchased the day before.

The Respondent knew that MMRW market timed mutual funds, and specifically that it intended to market time funds in Mutual Fund A's complex through Hedge Fund PB and PH's accounts. He knew or should have known Hedge Fund PB, PH and N had common beneficial owners. Moreover, he understood that a client might be able to evade Mutual Fund A's restrictions by trading Mutual Fund A's funds in a different account after Mutual Fund A had restricted market timing in one account. He explained that when a client reached 10 exchanges with Mutual Fund A, the client opened another account to continue market timing funds in Mutual Fund A's complex.

In assisting MMRW with its market timing activity, the Respondent facilitated MMRW's deceptive conduct that evaded Mutual Fund A's restrictions. As a result of its deception, MMRW was able to execute 14 exchanges more than the limits established in Mutual Fund A's prospectus. MMRW thereby profited at the expense of fund investors.

f. Violation

NASD Conduct Rule 2110 requires a member firm and its associated persons to observe high standards of commercial honor and just and equitable principles of trade.

By virtue of the activities described above, the Respondent violated NASD Conduct Rule 2110.

WHEREAS, the proposed Conclusions of Law made by the Hearing Officer are correct and are hereby adopted as the Conclusions of Law of the Secretary of State:

1. The Department properly served the Notice of Hearing on Respondent on March 6, 2006.

2. The Secretary of State has jurisdiction over the subject matter hereof pursuant to the Act.

3. Because of Respondent's failure to timely file an answer, a special appearance or other responsive pleading in accordance with Section 13.1104;

   (a) the allegations contained in the Notice of Hearing are deemed admitted.

   (b) Respondent waived his right to hearing.

   (c) Respondent is subject to an Order of Default.

4. Because the Respondent failed to appear at the time and place set for hearing, in accordance with Section 130.1109, he:

   (a) Waived his right to present evidence, argue, object or cross examine witnesses; or

   (b) Otherwise participate at the hearing

5. Section 8.E(1)(j) of the Act provides, inter alia, that the registration of the salesperson may be revoked if the Secretary of State finds that such salesperson has been suspended by any self-regulatory organization registered under the Federal 1934 Act or Federal 1974 Act arising from any fraudulent or deceptive act or practice in violation of any rule, regulation or standard promulgated by the self-regulatory organization.

6. NASD is a self-regulatory organization as specified in Section 8.E(1)(j) of the Act.

7. Section 8.E(3) of the Act provides, inter alia, for withdrawal of an application for registration or withdrawal from registration as a salesperson, effective 30 days after receipt of an application to withdraw or within such shorter period of time as the Secretary of State may determine. It no proceeding is pending or instituted and withdrawal automatically becomes effective, the Secretary of State may nevertheless institute a revocation or suspension proceeding within 2 years after withdrawal became effective and enter a revocation or suspension order as of the last date on which registration was effective.

8. By virtue of the foregoing, the Respondent's registration in the State of Illinois is subject to revocation pursuant to Section 8.3(1)(j) of the Act.

9. No showing of scienter or willful conduct is required to impose the requested sanction under Section 8.3(1)(j) of the Act.

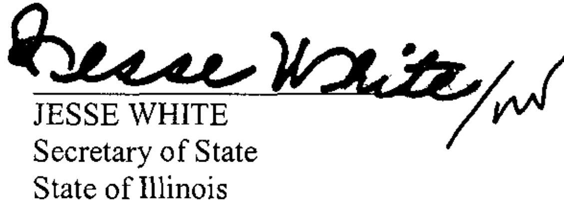
WHEREAS, the Hearing Officer recommended that the Secretary of State should revoke the Respondent's registration as a salesperson in the State of Illinois effective May 6, 2005, and the **Secretary of State adopts** in it's entirety the Recommendation made by the Hearing Officer.

NOW THEREFORE, IT SHALL BE AND IS HEREBY ORDERED THAT:

1. Respondent Gary N. Ferraro's registration as a salesperson in the State of Illinois is **REVOKED** effective February 18, 2004 pursuant to the authority found under Section 8.E(1)(j) and 8.E(3) of the Act.

2. This matter is concluded without further proceedings.

ENTERED This 27th day of June 2006.



JESSE WHITE
Secretary of State
State of Illinois

This is a final order subject to administrative review pursuant to the Administrative Review Law [735 ILCS 5/3-101 et seg.] and the Rules and Regulations of the Act (14 Ill. Admin. Code, Ch. 1 Sec. 130.1123). Any action for judicial review must be commenced within thirty-five (35) days from the date a copy of this Order is served upon the party seeking review.