

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-72382; File No. SR-NASDAQ-2014-041)

June 12, 2014

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, to List and Trade of Shares of the First Trust Enhanced Short Maturity ETF of First Trust Exchange-Traded Fund IV

I. Introduction

On April 11, 2014, The NASDAQ Stock Market LLC (“Exchange” or “Nasdaq”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change relating to the listing and trading of shares (“Shares”) of the First Trust Enhanced Short Maturity ETF (“Fund”) of First Trust Exchange-Traded Fund IV (“Trust”). On April 24, 2014, the Exchange filed Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission published for comment in the Federal Register notice of the proposed rule change, as modified by Amendment No. 1 thereto, on May 1, 2014.<sup>4</sup> The Commission received no comments on the proposed rule change. This order approves the proposed rule change, as modified by Amendment No. 1 thereto.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> In Amendment No. 1, the Exchange: (1) clarified that the Fund (defined below) will limit its investments in asset-backed securities and non-agency mortgage-backed securities (in the aggregate) to 20% of its net assets; (2) modified its description of how asset-backed or mortgage-backed securities will be priced in certain circumstances; and (3) made certain grammatical corrections.

<sup>4</sup> See Securities Exchange Act Release No. 72030 (April 25, 2014), 79 FR 24765 (“Notice”).

## II. Description of the Proposed Rule Change

The Exchange proposes to list and trade Shares pursuant to Nasdaq Rule 5735, which governs the listing and trading of Managed Fund Shares.<sup>5</sup> The Exchange deems the Shares to be equity securities, rendering trading in the Shares subject to the Exchange's existing rules governing the trading of equity securities.<sup>6</sup>

The Shares will be offered by the Trust, which is organized as a Massachusetts business trust and is registered with the Commission as an investment company.<sup>7</sup> First Trust Advisors L.P. is the investment adviser ("Adviser") to the Fund. First Trust Portfolios L.P. is the principal underwriter and distributor of the Shares ("Distributor"). The Bank of New York Mellon Corporation will act as the administrator, accounting agent, custodian, and transfer agent to the Fund. The Adviser is affiliated with the Distributor, a broker-dealer. As required by Nasdaq

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<sup>5</sup> Under Nasdaq's Rules, a Managed Fund Share is a security that (a) represents an interest in a registered investment company ("Investment Company") organized as an open-end management investment company or similar entity, that invests in a portfolio of securities selected by the Investment Company's investment adviser consistent with the Investment Company's investment objectives and policies; (b) is issued in a specified aggregate minimum number in return for a deposit of a specified portfolio of securities and/or a cash amount with a value equal to the next determined net asset value; and (c) when aggregated in the same specified minimum number, may be redeemed at a holder's request, which holder will be paid a specified portfolio of securities and/or cash with a value equal to the next determined net asset value. See Nasdaq Rule 5735(c)(1).

<sup>6</sup> See Notice, supra note 4, 79 FR at 24770.

<sup>7</sup> The Trust is registered under the Investment Company Act of 1940 ("1940 Act"). See Post-Effective Amendment No. 66 to Registration Statement on Form N-1A for the Trust, dated April 10, 2014 (File Nos. 333-174332 and 811-22559) ("Registration Statement"). The Exchange represents that the Trust has obtained certain exemptive relief under the 1940 Act. See Investment Company Act Release No. 30029 (April 10, 2012) (File No. 812-13795) ("Exemptive Order").

Rule 5735(g),<sup>8</sup> the Adviser has implemented a firewall with respect to its broker-dealer affiliate regarding access to information concerning the composition of or changes to the portfolio.<sup>9</sup>

First Trust Enhanced Short Maturity ETF<sup>10</sup>

The investment objective of the Fund will be to seek current income, consistent with preservation of capital and daily liquidity. Under normal market conditions,<sup>11</sup> the Fund will seek to achieve its investment objective by investing in a portfolio of U.S. dollar-denominated fixed- and variable-rate<sup>12</sup> instruments (collectively, “Fixed Income Securities”) issued by U.S. and non-

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<sup>8</sup> Nasdaq Rule 5735(g) also requires that Adviser personnel who make decisions regarding the Fund’s portfolio be subject to procedures designed to prevent the use and dissemination of material, non-public information regarding the Fund’s portfolio.

<sup>9</sup> Additionally, the Exchange represents that, in the event (a) the Adviser becomes newly affiliated with a broker-dealer, or (b) any new adviser or sub-adviser becomes affiliated with a broker-dealer, it will implement a fire wall with respect to such broker-dealer regarding access to information concerning the composition of or changes to the portfolio, and it will be subject to procedures designed to prevent the use and dissemination of material, non-public information regarding such portfolio.

<sup>10</sup> Additional information regarding the Trust, the Fund, and the Shares, including investment strategies, risks, creation and redemption procedures, fees, Fund holdings disclosure policies, distributions and taxes, among other things, is included in the Notice and Registration Statements, as applicable. See Notice and Registration Statement, supra notes 4 and 7, respectively.

<sup>11</sup> According to the Exchange, the term “under normal market conditions includes, but is not limited to, the absence of adverse market, economic, political or other conditions, including extreme volatility or trading halts in the fixed income markets or the financial markets generally; operational issues causing dissemination of inaccurate market information; or force majeure type events such as systems failure, natural or man-made disaster, act of God, armed conflict, act of terrorism, riot or labor disruption or any similar intervening circumstance. For temporary defensive purposes, during the initial invest-up period and during periods of high cash inflows or outflows, the Fund may depart from its principal investment strategies; for example, it may hold a higher than normal proportion of its assets in cash. During such periods, the Fund may not be able to achieve its investment objective. The Fund may adopt a defensive strategy when the Adviser believes securities in which the Fund normally invests have elevated risks due to political or economic factors and in other extraordinary circumstances.

<sup>12</sup> For these purposes, the term “variable-rate” also includes similar terms such as “floating-rate” and “adjustable-rate.”

U.S. public- and private-sector entities. The Fund will hold Fixed Income Securities of at least 13 non-affiliated issuers.

### Principal Investments

The Fund intends to achieve its investment objective by investing, under normal market conditions, at least 80% of its net assets in a portfolio of U.S. dollar-denominated Fixed Income Securities issued by U.S. and non-U.S. public- and private-sector entities. At least 80% of the Fund's net assets will be invested in Fixed Income Securities that are, at the time of purchase, investment grade. Fixed Income Securities will include the following types of fixed- and variable-rate debt securities: corporate<sup>13</sup> and government bonds and notes; agency securities; instruments of non-U.S. issuers in developed markets; privately-issued securities;<sup>14</sup> asset-backed securities;<sup>15</sup> mortgage-backed securities;<sup>16</sup> municipal bonds; money market securities; and investment companies<sup>17</sup> (including investment companies advised by the Adviser) that invest primarily in the foregoing types of Fixed Income Securities. The Fund will limit its investments

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<sup>13</sup> While the Fund is permitted to invest without restriction in corporate bonds, the Adviser expects that, under normal market conditions, generally, with respect to at least 75% of the Fund's portfolio, a corporate bond will have, at the time of original issuance, \$100 million or more par amount outstanding to be considered as an eligible investment.

<sup>14</sup> "Privately-issued securities" for these purposes generally includes Rule 144A securities and, in this context, may include both mortgage-backed and non-mortgage Rule 144A securities.

<sup>15</sup> Asset-backed securities are Fixed Income Securities that are backed by a pool of assets. The Fund currently intends to invest in asset-backed securities that are consumer asset-backed securities.

<sup>16</sup> Mortgage-backed securities are Fixed Income Securities that are backed by a pool of mortgage loans. There are a wide variety of mortgage-backed securities involving commercial or residential, fixed-rate or adjustable-rate mortgages and mortgages issued by banks or government agencies.

<sup>17</sup> Currently, the Fund anticipates investing only in registered open-end investment companies that are listed and traded in the U.S. on registered exchanges (i.e., other exchange traded funds).

in asset-backed securities and non-agency mortgage-backed securities (in the aggregate) to 20% of its net assets.<sup>18</sup>

Under normal market conditions, the Fund's duration<sup>19</sup> is expected to be below one year and the maturity<sup>20</sup> of the Fund's portfolio is expected to be below three years.

#### Other Investments

Under normal market conditions, the Fund will invest primarily in the Fixed Income Securities described above to meet its investment objective. In addition, the Fund may invest up to 20% of its net assets in floating rate loans. The floating rate loans in which the Fund will invest will represent amounts borrowed by companies or other entities from banks and other lenders and a significant portion of such floating rate loans may be rated below investment grade or unrated. Floating rate loans held by the Fund may be senior or subordinate obligations of the borrower and may or may not be secured by collateral.

#### Investment Restrictions

The Fund will not invest 25% or more of the value of its total assets in securities of issuers in any one industry. This restriction does not apply to (a) obligations issued or

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<sup>18</sup> See Amendment No. 1, supra note 3. There is no limit applicable to agency mortgage-backed securities.

<sup>19</sup> Duration is a measure of the expected price volatility of a debt instrument as a result of changes in market rates of interest, based on, among other factors, the weighted average timing of the instrument's expected principal and interest payments. Duration differs from maturity in that it considers a security's yield, coupon payments, principal payments, call features and coupon adjustments in addition to the amount of time until the security finally matures.

<sup>20</sup> Maturity is measured relative to the type of security. For Fixed Income Securities (exclusive of asset-backed securities and mortgage-backed securities), maturity shall be calculated using dollar-weighted average maturity, which is calculated by taking the average length of time to maturity. For asset-backed securities and mortgage-backed securities, maturity shall be calculated using weighted average life, which is the estimated time to principal paydown for each underlying instrument held by the Fund, weighted according to the relative holdings per instrument.

guaranteed by the U.S. government, its agencies or instrumentalities or (b) securities of other investment companies.

The Fund may hold up to an aggregate amount of 15% of its net assets in illiquid assets (calculated at the time of investment), including Rule 144A securities deemed illiquid by the Adviser. The Fund will monitor its portfolio liquidity on an ongoing basis to determine whether, in light of current circumstances, an adequate level of liquidity is being maintained, and will consider taking appropriate steps in order to maintain adequate liquidity if, through a change in values, net assets, or other circumstances, more than 15% of the Fund's net assets are held in illiquid assets. Illiquid assets include securities subject to contractual or other restrictions on resale and other instruments that lack readily available markets as determined in accordance with Commission staff guidance.<sup>21</sup>

The Fund will not invest in non-U.S. equity securities.

### III. Discussion and Commission's Findings

After careful review, the Commission finds that the proposed rule change, as modified by Amendment No. 1 thereto, is consistent with the requirements of Section 6 of the Act<sup>22</sup> and the rules and regulations thereunder applicable to a national securities exchange.<sup>23</sup> In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>24</sup> which requires, among other things, that the Exchange's rules be designed to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. The

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<sup>21</sup> See Notice, supra note 4, 79 FR at 24768, n.26.

<sup>22</sup> 15 U.S.C. 78f.

<sup>23</sup> In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>24</sup> 17 U.S.C. 78f(b)(5).

Commission notes that the Fund and the Shares will be listed and traded on the Exchange pursuant to the initial and continued listing criteria in Nasdaq's Rule 5735.

The Commission finds that the proposal to list and trade the Shares on the Exchange is consistent with Section 11A(a)(1)(C)(iii) of the Act,<sup>25</sup> which sets forth Congress' finding that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure the availability to brokers, dealers, and investors of information with respect to quotations for, and transactions in, securities. Information regarding market price and trading volume of the Shares will be continually available on a real-time basis throughout the day on brokers' computer screens and other electronic services. Quotation and last-sale information for the Shares will be available via Nasdaq proprietary quote and trade services, as well as in accordance with the Unlisted Trading Privileges and the Consolidated Tape Association plans for the Shares. Intraday executable price quotations on Fixed Income Securities and other assets not traded on an exchange will be available from major broker-dealer firms or market data vendors, as well as from automated quotation systems, published or other public sources, or online information services. For exchange-listed assets, intraday pricing information will be available directly from the applicable listing exchange. Intraday price information will also be available through subscription services, such as Bloomberg, Markit, and Thomson Reuters, which can be accessed by authorized participants and other investors.

The Commission believes that the proposal to list and trade the Shares is reasonably designed to promote fair disclosure of information that may be necessary to price the Shares appropriately and to prevent trading when a reasonable degree of transparency cannot be assured. The NAV of the Shares generally will be calculated once daily Monday through Friday as of the

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<sup>25</sup> 15 U.S.C. 78k-1(a)(1)(C)(iii).

close of regular trading on the New York Stock Exchange, generally 4:00 p.m., Eastern time. On each business day, before commencement of trading in Shares in the Regular Market Session<sup>26</sup> on the Exchange, the Fund will disclose on its website the identities and quantities of the portfolio of securities and other assets (“Disclosed Portfolio” as defined in Nasdaq Rule 5735(c)(2)) held by the Fund that will form the basis for the Fund’s calculation of NAV at the end of the business day.<sup>27</sup> The Exchange will obtain a representation from the issuer of the Shares that the NAV per Share will be calculated daily and that the NAV and the Disclosed Portfolio will be made available to all market participants at the same time.<sup>28</sup> Moreover, the Intraday Indicative Value, available on the NASDAQ OMX Information LLC proprietary index data service, will be widely disseminated by one or more major market data vendors and broadly displayed at least every 15 seconds during the Regular Market Session.<sup>29</sup> Trading in Shares will be halted if the circuit breaker parameters in Nasdaq Rule 4120(a)(11) have been reached or because of market conditions or for reasons that, in the view of the Exchange, make trading in the Shares inadvisable, and trading in the Shares will be subject to Nasdaq Rule 5735(d)(2)(D), which sets forth circumstances under which trading in the Shares may be halted. The Exchange states that it has a general policy prohibiting the distribution of material, non-public information by its employees. Further, the Commission notes that the Reporting Authority that provides the

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<sup>26</sup> See Nasdaq Rule 4120(b)(4) (describing the three trading sessions on the Exchange: (1) Pre-Market Session from 4 a.m. to 9:30 a.m., Eastern time; (2) Regular Market Session from 9:30 a.m. to 4 p.m. or 4:15 p.m., Eastern time; and (3) Post-Market Session from 4 p.m. or 4:15 p.m. to 8 p.m., Eastern time).

<sup>27</sup> Under accounting procedures to be followed by the Fund, trades made on the prior business day (“T”) will be booked and reflected in NAV on the current business day (“T+1”). Accordingly, the Fund will be able to disclose at the beginning of the business day the portfolio that will form the basis for the NAV calculation at the end of the business day.

<sup>28</sup> See Notice, supra note 4, 79 FR at 24770.

<sup>29</sup> See id.



Disclosed Portfolio must implement and maintain, or be subject to, procedures designed to prevent the use and dissemination of material, non-public information regarding the actual components of the portfolio.<sup>30</sup> The Adviser is affiliated with a broker-dealer and has implemented a firewall with respect to that broker-dealer regarding access to information concerning the composition and/or changes to the Fund's portfolio.<sup>31</sup>

Further, regarding trading in the Shares and the exchange-traded securities held by the Fund, the Commission notes that the Financial Industry Regulatory Authority ("FINRA") will communicate as needed on behalf of the Exchange<sup>32</sup> with other markets and other entities that are members of the Intermarket Surveillance Group ("ISG"),<sup>33</sup> and FINRA may obtain trading information regarding trading in the Shares and the exchange-traded securities held by the Fund from such markets and other entities that are members of the ISG, which includes securities and futures exchanges, or from markets which the Exchange has in place a comprehensive surveillance sharing agreement.<sup>34</sup> Moreover, the Exchange states that FINRA will be able to access on its behalf, as needed, trade information for certain Fixed Income Securities held by the Fund reported to FINRA's Trade Reporting and Compliance Engine.<sup>35</sup> The Exchange states that trading in the Shares will be subject to the existing trading surveillances, administered by FINRA

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<sup>30</sup> See Nasdaq Rule 5735(d)(2)(B)(ii).

<sup>31</sup> See note 9, supra and accompanying text.

<sup>32</sup> The Exchange states that, while FINRA surveils trading on the Exchange pursuant to a regulatory services agreement, the Exchange is responsible for FINRA's performance under this regulatory services agreement. See Notice, supra note 4, 79 FR at 24771, n.34.

<sup>33</sup> For a list of the current members of ISG, see [www.isgportal.org](http://www.isgportal.org). The Exchange states that not all components of the Disclosed Portfolio may trade on markets that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement. See id. at 24771, n.35.

<sup>34</sup> See id. at 24771.

<sup>35</sup> See id.

on behalf of the Exchange, which are designed to detect violations of Exchange rules and applicable federal securities laws, and represents that these procedures are adequate to properly monitor Exchange trading of the Shares in all trading sessions and to deter and detect violations of Exchange rules and applicable federal securities laws.<sup>36</sup>

In support of this proposal, the Exchange has made representations, including:

(1) The Shares will conform to the initial and continued listing criteria under Nasdaq Rule 5735.

(2) The Exchange has appropriate rules to facilitate transactions in the Shares during all trading sessions.

(3) The Exchange represents that trading in the Shares will be subject to the existing trading surveillances, administered by FINRA on behalf of the Exchange, which are designed to detect violations of Exchange rules and applicable federal securities laws and that these procedures are adequate to properly monitor Exchange trading of the Shares in all trading sessions and to deter and detect violations of Exchange rules and applicable federal securities laws.

(4) Prior to the commencement of trading, the Exchange will inform its members in an Information Circular of the special characteristics and risks associated with trading the Shares. Specifically, the Information Circular will discuss the following: (a) the procedures for purchases and redemptions of Shares in Creation Units (and that Shares are not individually redeemable); (b) Nasdaq Rule 2310, which imposes suitability obligations on Nasdaq members with respect to recommending transactions in the Shares to customers; (c) how information regarding the Intraday Indicative Value is disseminated; (d) the risks involved in trading the

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<sup>36</sup> See id. at 24770-71.

Shares during the Pre-Market and Post-Market Sessions when an updated Intraday Indicative Value will not be calculated or publicly disseminated; (e) the requirement that members deliver a prospectus to investors purchasing newly issued Shares prior to or concurrently with the confirmation of a transaction; and (f) trading information.<sup>37</sup>

(5) For initial and continued listing, the Fund will be in compliance with Rule 10A-3 under the Act.<sup>38</sup>

(6) While the Fund is permitted to invest without restriction in corporate bonds, the Adviser expects that, under normal market conditions, generally, with respect to at least 75% of the Fund's portfolio, a corporate bond will have, at the time of original issuance, \$100 million or more par amount outstanding to be considered as an eligible investment.

(7) The Fund may hold up to an aggregate amount of 15% of its net assets in illiquid assets (calculated at the time of investment), including Rule 144A securities deemed illiquid by the Adviser.

(8) The Fund will limit its investments in asset-backed securities and non-agency mortgage-backed securities (in the aggregate) to 20% of its net assets.

(9) The Fund will not invest in non-U.S. equity securities.

(10) A minimum of 100,000 Shares will be outstanding at the commencement of trading

This approval order is based on all of the Exchange's representations, including those set forth in the Notice.

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<sup>37</sup> See id. at 24771.

<sup>38</sup> 17 CFR 240.10A-3.

IV. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act<sup>39</sup> and the rules and regulations thereunder applicable to a national securities exchange.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>40</sup> that the proposed rule change (SR-NASDAQ-2014-041), as modified by Amendment No. 1, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>41</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>39</sup> 15 U.S.C. 78f(b)(5).

<sup>40</sup> 15 U.S.C. 78s(b)(2).

<sup>41</sup> 17 CFR 200.30-3(a)(12).