

FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC

Form N-30B-2

October 28, 2010

FLAHERTY & CRUMRINE PREFERRED INCOME FUND

To the Shareholders of Flaherty & Crumrine Preferred Income Fund:

The combination of falling interest rates and ongoing demand for preferred securities helped the Fund produce excellent returns during its third fiscal period ending August 31, 2010. For the three month period, total return on net asset value was +12.1%. Total return using market price of Fund shares was +18.5% during the period.

It has been quite an eventful summer in the preferred securities market. We'll hit the highlights here, and readers willing to do a little extra-credit homework will find more detailed discussions on the Fund's website.

In addition to strong performance of the Fund's investment portfolio, the monthly dividend paid to shareholders was increased to \$0.089 per share from \$0.0825, commencing with the August distribution. This 7.9% increase reflects the ongoing favorable environment of relatively high yields on Fund investments and the low cost of Fund borrowings.

We expect the level of economic growth to remain tepid over the coming quarters and then to show gradual improvement. We anticipate the Fund's cost of borrowing will follow a similar path, remaining low for a period, then increasing gradually. Of course, unless income from the Fund's investments also increases, a rise in the cost of borrowing would negatively impact the distribution to shareholders.

Although economic activity has slowed recently, we do not expect the economy to fall back into recession. In fact, we see some healthy signs, such as a substantial increase in personal savings and steady levels of business investment aimed at improving productivity. As individuals save more, some of these dollars are likely to find their way into the preferred market. As companies become more efficient, their financial condition generally improves. These trends, along with declining interest rates, have helped boost the Fund's investment performance.

In the aftermath of the financial meltdown, Congress and various bank regulators set out to establish new rules to hopefully prevent a repeat of the crisis. We are now getting a better sense of how new regulations will impact the market. With passage of the Dodd-Frank Wall Street Reform and Consumer Protection Act in July, along with increasing clarification from international bank regulators, the fog is beginning to lift on the future role of preferred securities as a source of capital for the banking industry(1).

Since our last letter, rule makers have indicated which security structures they don't like, but have yet to decide what will be okay. It is now clear that trust preferred securities, which are favored by banks as a form of capital, will not meet the new standards. As a result, not only will there be no new issues of this type, issuers will want to redeem or replace outstanding trust preferreds sooner than was previously expected. In response, prices of many bank trust preferred securities have moved higher--contributing to the Fund's strong performance.

It is less clear what types of securities banks will be allowed to issue to meet future capital requirements. We are monitoring the debate closely and throwing in our two cents whenever appropriate. At this time, we believe the parties are moving toward a sensible conclusion and will ultimately induce banks

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to issue preferred securities suitable for the Fund's portfolio. Of course, we will stay on top of this and report important developments in these letters or on the Fund's website.

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- (1) The treatment of preferred securities issued by NON-BANKS has not changed in any meaningful way.

As of this writing, roughly 23% of the Fund's portfolio is invested in trust preferred securities issued by U.S. banks. In light of the new rules, we think it is likely that many of these issues will be redeemed, beginning in 2013. We'll have our work cut out for us trying to replace the income on these securities, but until we have a better idea how the banks will replace these issues, it is difficult to predict the impact on the Fund.

As always, we encourage you to visit [www.pfdincome.com](http://www.pfdincome.com) to read our Quarterly Economic Update as well as a more detailed discussion of factors affecting the wonderful world of preferred securities.

Sincerely,

/s/ Donald F. Crumrine

/s/ Robert M. Ettinger

Donald F. Crumrine  
Chairman

Robert M. Ettinger  
President

October 15, 2010

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Flaherty & Crumrine Preferred Income Fund Incorporated  
PORTFOLIO OVERVIEW  
AUGUST 31, 2010 (UNAUDITED)

### FUND STATISTICS

-----

|                                 |    |            |
|---------------------------------|----|------------|
| Net Asset Value                 | \$ | 11.49      |
| Market Price                    | \$ | 12.37      |
| Premium                         |    | 7.66%      |
| Yield on Market Price           |    | 8.63%      |
| Common Stock Shares Outstanding |    | 10,734,121 |

### MOODY'S RATINGS

-----

### % OF NET ASSETS+

-----

|            |       |
|------------|-------|
| A          | 6.5%  |
| BBB        | 71.4% |
| BB         | 19.4% |
| Below "BB" | 0.6%  |
| Not Rated* | 0.3%  |

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Below Investment Grade\*\* 15.2%

\* Does not include net other assets and liabilities of 1.8%.

\*\* Below investment grade by both Moody's and S&P.

(PIE CHART)

| INDUSTRY CATEGORIES | % OF NET ASSETS+ |
|---------------------|------------------|
| Banking             | 40%              |
| Utilities           | 25%              |
| Insurance           | 22%              |
| Energy              | 6%               |
| Financial Services  | 2%               |
| Other               | 5%               |

| TOP 10 HOLDINGS BY ISSUER | % OF NET ASSETS+ |
|---------------------------|------------------|
| Banco Santander           | 5.6%             |
| Capital One Financial     | 4.2%             |
| PNC Financial Services    | 4.1%             |
| Liberty Mutual Group      | 4.0%             |
| Comerica                  | 3.7%             |
| Dominion Resources        | 3.3%             |
| Wells Fargo               | 3.2%             |
| HSBC Plc                  | 3.1%             |
| Interstate Power & Light  | 3.0%             |
| Metlife                   | 3.0%             |

|  | % OF NET ASSETS***+ |
|--|---------------------|
| Holdings Generating Qualified Dividend Income (QDI) for Individuals                      | 41%                 |
| Holdings Generating Income Eligible for the Corporate Dividends Received Deduction (DRD) | 26%                 |

\*\*\* This does not reflect year-end results or actual tax categorization of Fund distributions. These percentages can, and do, change, perhaps significantly, depending on market conditions. Investors should consult their tax advisor regarding their personal situation.

+ Net Assets includes assets attributable to the use of leverage.

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS  
 AUGUST 31, 2010 (UNAUDITED)

SHARES/\$ PAR

PREFERRED SECURITIES -- 95.2%

BANKING -- 39.8%

|             |   |
|-------------|---|
| \$2,750,000 | Astoria Capital Trust I, 9.75% 11/01/29, Series B .....                               |
| 355,000     | Banco Santander, 10.50% Pfd., Series 10 .....   |
| 48,700      | Bank of America Corporation, 6.70% Pfd. ....  |
| \$ 500,000  | BankAmerica Institutional, Series A, 8.07% 12/31/26, 144A**** .....                   |
|             | Barclays Bank PLC:  |
| \$3,000,000 | 6.278% .....  |
| 40,000      | 6.625% Pfd., Series 2 .....   |
| 6,200       | 7.75% Pfd., Series 4 .....  |
| 35,000      | 8.125% Pfd., Series 5 .....   |
| 87,500      | BB&T Capital Trust VI, 9.60% Pfd. ....  |
| \$4,500,000 | Capital One Capital III, 7.686% 08/15/36 .....  |
| \$ 500,000  | Capital One Capital V, 10.25% 08/15/39 .....  |
| \$2,500,000 | Capital One Capital VI, 8.875% 05/15/40 .....   |
| \$5,210,000 | Colonial BancGroup, 7.114%, 144A**** .....  |
| \$7,250,000 | Comerica Capital Trust II, 6.576% 02/20/37 .....                                      |
| 9,000       | FBOP Corporation, Adj. Rate Pfd., 144A**** .....                                      |
| \$ 750,000  | Fifth Third Capital Trust IV, 6.50% 04/15/37 .....                                    |
| 15,000      | Fifth Third Capital Trust V, 7.25% Pfd. 08/15/67 .....                                |
| 14,500      | Fifth Third Capital Trust VII, 8.875% Pfd. 05/15/68 .....                             |
| 1,250       | First Republic Preferred Capital Corporation, 10.50% Pfd., 144A**** .....             |
| 22,500      | First Republic Preferred Capital Corporation II, 8.75% Pfd., Series B, 144A**** ..... |
| 3,750       | First Tennessee Bank, Adj. Rate Pfd., 144A**** .....                                  |
| \$ 600,000  | First Tennessee Capital I, 8.07% 01/06/27, Series A .....                             |
| \$ 500,000  | First Tennessee Capital II, 6.30% 04/15/34, Series B .....                            |
| \$1,500,000 | First Union Capital II, 7.95% 11/15/29 .....  |
| \$1,000,000 | First Union Institutional Capital I, 8.04% 12/01/26 .....                             |
| \$ 500,000  | Fleet Capital Trust II, 7.92% 12/11/26 .....  |
|             | Goldman Sachs:  |
| \$ 500,000  | Capital I, 6.345% 02/15/34 .....  |
| \$3,713,000 | Capital II, 5.793% .....  |
| 2,500       | STRIPES Custodial Receipts, Pvt. ....   |
| 135,000     | HSBC Holdings PLC, 8.00% Pfd., Series 2 .....   |
| \$ 500,000  | HSBC USA Capital Trust II, 8.38% 05/15/27, 144A**** .....                             |
|             | HSBC USA, Inc.:   |
| 48,000      | 6.50% Pfd., Series H .....  |
| 4,400       | \$2.8575 Pfd. ....  |
| \$ 300,000  | JPMorgan Chase Capital XVIII, 6.95% 08/17/36, Series R .....                          |
| 15,000      | Keycorp Capital VIII, 7.00% Pfd. 06/15/66 .....                                       |

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2010 (UNAUDITED)

SHARES/\$ PAR

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 PREFERRED SECURITIES -- (CONTINUED)

BANKING -- (CONTINUED)

|             |  |
|-------------|--|
| 27,600      | Keycorp Capital X, 8.00% Pfd. ....                     |
| \$ 550,000  | Lloyds Banking Group PLC, 6.657%, 144A**** .....       |
| \$ 600,000  | NB Capital Trust IV, 8.25% 04/15/27 .....              |
| 200,000     | PNC Financial Services, 9.875% Pfd., Series F .....    |
| \$1,750,000 | PNC Preferred Funding Trust III, 8.70%, 144A**** ..... |
| 1,750       | Sovereign REIT, 12.00% Pfd., Series A, 144A**** .....  |
| \$2,400,000 | Wachovia Capital Trust III, 5.80% .....                |
| \$1,000,000 | Washington Mutual, 9.75%, 144A**** .....               |
| \$1,600,000 | Webster Capital Trust IV, 7.65% 06/15/37 .....         |
| \$1,000,000 | Wells Fargo Capital XV, 9.75% .....                    |

FINANCIAL SERVICES -- 2.0%

|        |  |
|--------|--|
| 5,000  | Deutsche Bank Contingent Capital Trust II, 6.55% Pfd ..... |
| 33,000 | Heller Financial, Inc., 6.687% Pfd., Series C .....        |
| 10,300 | HSBC Finance Corporation, 6.36% Pfd .....                  |
|        | Lehman Brothers Holdings, Inc.:                            |
| 15,000 | 5.67% Pfd., Series D .....                                 |
| 19,500 | 5.94% Pfd., Series C .....                                 |
| 25,000 | 6.50% Pfd., Series F .....                                 |
| 27,500 | 7.95% Pfd .....  |

INSURANCE -- 19.8%

|             |   |
|-------------|---|
| \$ 750,000  | Ace Capital Trust II, 9.70% 04/01/30 .....              |
| \$ 250,000  | AON Corporation, 8.205% 01/01/27 .....                  |
| 25,000      | Arch Capital Group Ltd., 8.00% Pfd., Series A .....     |
|             | AXA SA:   |
| \$1,750,000 | 6.379%, 144A**** .....                                  |
| \$3,000,000 | 6.463%, 144A**** .....                                  |
| 35,900      | Axis Capital Holdings, 7.50% Pfd., Series B .....       |
| 90,600      | Delphi Financial Group, 7.376% Pfd. 05/15/37 .....      |
| \$4,000,000 | Everest Re Holdings, 6.60% 05/15/37 .....               |
|             | Liberty Mutual Group:                                   |
| \$ 500,000  | 7.80% 03/15/37, 144A**** .....                          |
| \$4,100,000 | 10.75% 06/15/58, 144A**** .....                         |
| \$2,100,000 | MetLife Capital Trust X, 9.25% 04/08/38, 144A**** ..... |

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2010 (UNAUDITED)

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PREFERRED SECURITIES -- (CONTINUED)  
 INSURANCE -- (CONTINUED)

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|             |   |
|-------------|---|
| \$2,400,000 | MetLife, Inc., 10.75% 08/01/39 .....                            |
|             | Principal Financial Group:                                      |
| 16,000      | 5.563% Pfd., Series A .....                                     |
| 70,000      | 6.518% Pfd., Series B .....                                     |
|             | Renaissancere Holdings Ltd.:                                    |
| 131,450     | 6.08% Pfd., Series C .....                                      |
| 6,900       | 7.30% Pfd., Series B .....                                      |
| 119,500     | Scottish Re Group Ltd., 7.25% Pfd. ....                         |
| \$1,300,000 | Stancorp Financial Group, 6.90% 06/01/67 .....                  |
| \$ 750,000  | USF&G Capital, 8.312% 07/01/46, 144A**** .....                  |
| \$2,000,000 | XL Capital Ltd., 6.50%, Series E .....                          |
| \$1,000,000 | ZFS Finance USA Trust V, 6.50% 05/09/37, 144A****               |
|             | UTILITIES -- 25.1%  |
| 10,000      | Baltimore Gas & Electric Company, 6.70% Pfd., Series 1993 ..... |
| \$3,458,000 | COMED Financing III, 6.35% 03/15/33 .....                       |
| \$ 250,000  | Dominion Resources Capital Trust I, 7.83% 12/01/27 .....        |
|             | Dominion Resources, Inc.:                                       |
| \$3,500,000 | 7.50% .....   |
| 77,000      | 8.375% Pfd., Series A .....                                     |
| 40,000      | Entergy Arkansas, Inc., 6.45% Pfd. ....                         |
| 20,000      | Entergy Louisiana, Inc., 6.95% Pfd. ....                        |
| \$2,000,000 | FPL Group Capital, Inc., 6.65% 06/15/67 .....                   |
|             | Georgia Power Company:  |
| 5,000       | 6.125% Pfd .....  |
| 25,000      | 6.50% Pfd., Series 2007A .....                                  |
| 3,000       | Gulf Power Company, 6.45% Pfd., Series 2007A .....              |
| 32,650      | Indianapolis Power & Light Company, 5.65% Pfd. ....             |
| 190,000     | Interstate Power & Light Company, 8.375% Pfd., Series B .....   |
| 7,146       | MDU Resources Group, 4.50% Pfd. 07/08/10 .....                  |
| 22,430      | Pacific Enterprises, \$4.50 Pfd. ....                           |
| \$ 500,000  | PECO Energy Capital Trust III, 7.38% 04/06/28, Series D .....   |
| \$4,400,000 | Puget Sound Energy, Inc., 6.974% 06/01/67 .....                 |
| 55,500      | Scana Corporation, 7.70% Pfd. ....                              |

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2010 (UNAUDITED)

SHARES/\$ PAR

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PREFERRED SECURITIES -- (CONTINUED)

UTILITIES -- (CONTINUED)

Southern California Edison:

|             |  |
|-------------|--|
| 32,100      | 6.00% Pfd., Series C .....                         |
| 17,500      | 6.125% Pfd .....                                   |
| \$3,000,000 | Southern Union Company, 7.20% 11/01/66 .....       |
| \$ 750,000  | TXU Electric Capital V, 8.175% 01/30/37 .....      |
| \$3,000,000 | Wisconsin Energy Corporation, 6.25% 05/15/67 ..... |
| 6,750       | Xcel Energy, Inc., \$4.08 Pfd., Series B .....     |

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|             |   |
|-------------|---|
|             | ENERGY -- 6.4%  |
| \$4,250,000 | Enbridge Energy Partners LP, 8.05% 10/01/37 .....         |
|             | Enterprise Products Partners:                             |
| \$ 750,000  | 7.00% 06/01/67 .....                                      |
| \$3,250,000 | 8.375% 08/01/66, Series A .....                           |
| 3,500       | Kinder Morgan GP, Inc., 8.33% Pfd., 144A**** .....        |
|             | REAL ESTATE INVESTMENT TRUST (REIT) -- 0.2%               |
| 12,500      | PS Business Parks, Inc., 6.70% Pfd., Series P .....       |
|             | MISCELLANEOUS INDUSTRIES -- 1.9%                          |
| 40,000      | Ocean Spray Cranberries, Inc., 6.25% Pfd., 144A**** ..... |
|             | TOTAL PREFERRED SECURITIES                                |
|             | (Cost \$170,603,149) .....                                |
|             | CORPORATE DEBT SECURITIES -- 2.9%                         |
|             | FINANCIAL SERVICES -- 0.2%                                |
| 10,000      | Ameriprise Financial, Inc., 7.75% 06/15/39 .....          |

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2010 (UNAUDITED)

SHARES/\$ PAR  
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|             |   |
|-------------|---|
|             | INSURANCE -- 2.4%   |
| \$2,500,000 | Liberty Mutual Insurance, 7.697% 10/15/97, 144A**** .....     |
| \$2,000,000 | UnumProvident Corporation, 7.25% 03/15/28, Senior Notes ..... |
|             | UTILITIES -- 0.3%   |
| 20,000      | Entergy Texas, Inc., 7.875% 06/01/39 .....                    |
|             | TOTAL CORPORATE DEBT SECURITIES                               |
|             | (Cost \$4,192,390) .....                                      |
|             | COMMON STOCK -- 0.1%  |
|             | BANKING -- 0.1%   |
| 3,620       | CIT Group, Inc. ....  |

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|   |           |
|---|-----------|
| TOTAL COMMON STOCK  |           |
| (Cost \$330,325) .....                                    |           |
| MONEY MARKET FUND -- 3.7%                                 |           |
| 6,874,830 BlackRock Provident Institutional, T-Fund ..... |           |
| TOTAL MONEY MARKET FUND                                   |           |
| (Cost \$6,874,830) .....                                  |           |
| TOTAL INVESTMENTS (Cost \$182,000,694***) .....           | 101.9%    |
| OTHER ASSETS AND LIABILITIES (Net) .....                  | (1.9)%    |
|   | -----     |
| NET ASSETS BEFORE LOAN .....                              | 100.0%+++ |
|   | -----     |
| LOAN PRINCIPAL BALANCE .....                              |           |
| TOTAL NET ASSETS AVAILABLE TO COMMON STOCK .....          |           |

-----  
 \* Securities eligible for the Dividends Received Deduction and distributing Qualified Dividend Income.

\*\* Securities distributing Qualified Dividend Income only.

\*\*\* Aggregate cost of securities held.

\*\*\*\* Securities exempt from registration under Rule 144A of the Securities Act of 1933. These securities may be resold in transactions exempt from registration to qualified institutional buyers. At August 31, 2010, these securities amounted to \$32,038,931 or 17.4% of net assets before loan. These securities have been determined to be liquid under the guidelines established by the Board of Directors.

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2010 (UNAUDITED)

(1) All or a portion of this security has been pledged as collateral for the Fund's loan. The total value of such securities was \$131,217,188 at August 31, 2010.

(2) Foreign Issuer.

+ Non-income producing.

++ The issuer has filed for bankruptcy protection. As a result, the Fund may not be able to recover the principal invested and also does not expect to receive income on this security going forward.

+++ The percentage shown for each investment category is the total value of that category as a percentage of net assets before the loan.

ABBREVIATIONS:

PFD. -- Preferred Securities  
 PVT. -- Private Placement Securities



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REIT -- Real Estate Investment Trust  
 STRIPES -- Structured Residual Interest Preferred Enhanced Securities

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 STATEMENT OF CHANGES IN NET ASSETS AVAILABLE TO COMMON STOCK(1)  
 FOR THE PERIOD FROM DECEMBER 1, 2009 THROUGH AUGUST 31, 2010 (UNAUDITED)

|   | VALUE         |
|---|---------------|
|   | -----         |
| OPERATIONS:   |               |
| Net investment income .....   | \$ 8,627,740  |
| Net realized gain/(loss) on investments sold during the period .....  | 1,558,215     |
| Change in net unrealized appreciation/depreciation of investments .....   | 15,197,346    |
| Distributions to APS* Shareholders from net investment income,<br>including changes in accumulated undeclared distributions ..... | (70,977)      |
|   | -----         |
| NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS .....  | 25,312,324    |
| DISTRIBUTIONS:  |               |
| Dividends paid from net investment income to Common Stock Shareholders(2) ...   | (7,454,757)   |
|   | -----         |
| TOTAL DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS .....  | (7,454,757)   |
| FUND SHARE TRANSACTIONS:  |               |
| Increase from shares issued under the Dividend Reinvestment and<br>Cash Purchase Plan .....                                       | 683,032       |
|   | -----         |
| NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK RESULTING FROM<br>FUND SHARE TRANSACTIONS .....                              | 683,032       |
|   | -----         |
| NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD .....   | \$ 18,540,599 |
|   | =====         |
| NET ASSETS AVAILABLE TO COMMON STOCK:   |               |
| Beginning of period .....   | \$104,764,121 |
| Net increase in net assets during the period .....  | 18,540,599    |
|   | -----         |
| End of period .....   | \$123,304,720 |
|   | =====         |

-----  
 \* Auction Preferred Stock.

(1) These tables summarize the nine months ended August 31, 2010 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2009.

(2) May include income earned, but not paid out, in prior fiscal year.

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 FINANCIAL HIGHLIGHTS(1)

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FOR THE PERIOD FROM DECEMBER 1, 2009 THROUGH AUGUST 31, 2010 (UNAUDITED)  
FOR A COMMON STOCK SHARE OUTSTANDING THROUGHOUT THE PERIOD.

PER SHARE OPERATING PERFORMANCE:

|  |    |       |
|--|----|-------|
| Net asset value, beginning of period ..... | \$ | 9.82  |
|  |    | ----- |

INVESTMENT OPERATIONS:

|  |  |      |
|--|--|------|
| Net investment income .....                                  |  | 0.81 |
| Net realized and unrealized gain/(loss) on investments ..... |  | 1.57 |

DISTRIBUTIONS TO APS\* SHAREHOLDERS:

|                                  |  |        |
|----------------------------------|--|--------|
| From net investment income ..... |  | (0.01) |
|                                  |  | -----  |

|  |  |       |
|--|--|-------|
| Total from investment operations ..... |  | 2.37  |
|  |  | ----- |

DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS:

|                                  |  |        |
|----------------------------------|--|--------|
| From net investment income ..... |  | (0.70) |
|                                  |  | -----  |

|  |  |        |
|--|--|--------|
| Total distributions to Common Stock Shareholders ..... |  | (0.70) |
|  |  | -----  |

|                                      |    |       |
|--------------------------------------|----|-------|
| Net asset value, end of period ..... | \$ | 11.49 |
|                                      |    | ===== |

|                                   |    |       |
|-----------------------------------|----|-------|
| Market value, end of period ..... | \$ | 12.37 |
|                                   |    | ===== |

|  |  |            |
|--|--|------------|
| Common Stock shares outstanding, end of period ..... |  | 10,734,121 |
|  |  | =====      |

RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:

|                              |  |         |
|------------------------------|--|---------|
| Net investment income+ ..... |  | 9.96%** |
|------------------------------|--|---------|

|  |  |         |
|--|--|---------|
| Net investment income, including payments to APS Shareholders+ ..... |  | 9.88%** |
|--|--|---------|

|   |  |         |
|---|--|---------|
| Operating expenses including interest expense ..... |  | 2.32%** |
|---|--|---------|

|   |  |         |
|---|--|---------|
| Operating expenses excluding interest expense ..... |  | 1.60%** |
|---|--|---------|

SUPPLEMENTAL DATA:++

|                               |  |       |
|-------------------------------|--|-------|
| Portfolio turnover rate ..... |  | 24%** |
|-------------------------------|--|-------|

|  |    |         |
|--|----|---------|
| Net assets before loan, end of period (in 000's) ..... | \$ | 183,805 |
|--|----|---------|

|  |  |         |
|--|--|---------|
| Ratio of operating expenses including interest expense(2) to net assets<br>before loan and APS ..... |  | 1.55%** |
|--|--|---------|

|  |  |         |
|--|--|---------|
| Ratio of operating expenses excluding interest expense(2) to net assets<br>before loan and APS ..... |  | 1.07%** |
|--|--|---------|

(1) These tables summarize the nine months ended August 31, 2010 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2009.

(2) Does not include distributions to APS Shareholders.

\* Auction Preferred Stock.

\*\* Annualized.

\*\*\* Not Annualized.

+ The net investment income ratios reflect income net of operating expenses, including interest expense.

++ Information presented under heading Supplemental Data includes APS and loan principal balance.

Flaherty & Crumrine Preferred Income Fund Incorporated  
 FINANCIAL HIGHLIGHTS (CONTINUED)  
 PER SHARE OF COMMON STOCK (UNAUDITED)

|                         | TOTAL<br>DIVIDENDS<br>PAID | NET ASSET<br>VALUE | NYSE<br>CLOSING PRICE | DIVIDEND<br>REINVESTMENT<br>PRICE (1) |
|-------------------------|----------------------------|--------------------|-----------------------|---------------------------------------|
|                         | -----                      | -----              | -----                 | -----                                 |
| December 31, 2009 ..... | \$0.0720                   | \$10.31            | \$10.47               | \$10.31                               |
| January 29, 2010 .....  | 0.0720                     | 10.52              | 10.59                 | 10.52                                 |
| February 26, 2010 ..... | 0.0720                     | 10.67              | 11.37                 | 10.80                                 |
| March 31, 2010 .....    | 0.0720                     | 11.08              | 11.32                 | 11.08                                 |
| April 30, 2010 .....    | 0.0720                     | 11.24              | 11.93                 | 11.33                                 |
| May 28, 2010 .....      | 0.0825                     | 10.48              | 10.67                 | 10.48                                 |
| June 30, 2010 .....     | 0.0825                     | 10.65              | 11.30                 | 10.74                                 |
| July 30, 2010 .....     | 0.0825                     | 11.15              | 12.33                 | 11.71                                 |
| August 31, 2010 .....   | 0.0890                     | 11.49              | 12.37                 | 11.75                                 |

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 (1) Whenever the net asset value per share of the Fund's Common Stock is less than or equal to the market price per share on the reinvestment date, new shares issued will be valued at the higher of net asset value or 95% of the then current market price. Otherwise, the reinvestment shares of Common Stock will be purchased in the open market.

Flaherty & Crumrine Preferred Income Fund Incorporated  
 NOTES TO FINANCIAL STATEMENTS (UNAUDITED)

1. AGGREGATE INFORMATION FOR FEDERAL INCOME TAX PURPOSES

At August 31, 2010, the aggregate cost of securities for federal income tax purposes was \$181,998,123, the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was \$26,736,042 and the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was \$21,433,060.

2. ADDITIONAL ACCOUNTING STANDARDS

FAIR VALUE MEASUREMENT: The inputs and valuation techniques used to measure fair value of the Fund's investments are summarized into three levels as described in the hierarchy below:

- Level 1 - quoted prices in active markets for identical securities
- Level 2 - other significant observable inputs (including quoted prices for similar securities, interest rates, prepayment speeds, credit risk, etc.)
- Level 3 - significant unobservable inputs (including the Fund's own assumptions in determining the fair value of investments)

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The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. Transfers in and out of levels are recognized at market value at the end of the period. A summary of the inputs used to value the Fund's investments as of August 31, 2010 is as follows:

|                                     | TOTAL<br>VALUE AT<br>AUGUST 31, 2010 | LEVEL 1<br>QUOTED<br>PRICE | LEVEL 2<br>SIGNIFICANT<br>OBSERVABLE<br>INPUTS | LEVEL<br>SIGNIFICANT<br>UNOBSERVABLE<br>INPUTS |
|-------------------------------------|--------------------------------------|----------------------------|--|--|
| Preferred Securities                |                                      |                            |  |  |
| Banking                             | \$ 73,150,901                        | \$44,448,294               | \$ 28,667,867                                  | \$34,744,427                                   |
| Financial Services                  | 3,588,795                            | 367,831                    | 3,220,964                                      | —  |
| Insurance                           | 36,489,347                           | 13,790,746                 | 22,698,601                                     | —  |
| Utilities                           | 46,141,294                           | 13,011,922                 | 33,129,372                                     | —  |
| Energy                              | 11,788,911                           | —                          | 11,788,911                                     | —  |
| Real Estate Investment Trust (REIT) | 302,156                              | 302,156                    | —  | —  |
| Miscellaneous Industries            | 3,520,000                            | —                          | 3,520,000                                      | —  |
| Corporate Debt Securities           | 5,312,089                            | 849,625                    | 4,462,464                                      | —  |
| Common Stock                        |                                      |                            |  |  |
| Banking                             | 132,782                              | 132,782                    | —  | —  |
| Money Market Fund                   | 6,874,830                            | 6,874,830                  | —  | —  |
| Total Investments                   | \$187,301,105                        | \$79,778,186               | \$107,488,179                                  | \$34,744,427                                   |

The Fund did not have any significant transfers in and out of Level 1 and Level 2 during the period.

Flaherty & Crumrine Preferred Income Fund Incorporated  
NOTES TO FINANCIAL STATEMENTS (UNAUDITED) (CONTINUED)

The Fund's investments in Level 2 and Level 3 are based primarily on market information, where available. This includes, but is not limited to, prices provided by third-party providers, observable trading activity (including the recency, depth, and consistency of such information with quoted levels), and the depth and consistency of broker-quoted prices. In the event market information is not directly available, comparable information may be observed for securities that are similar in many respects to those being valued. The Fund may employ an income approach for certain securities that also takes into account credit risk, interest rate risk, and potential recovery prospects.

The following is a reconciliation of Level 3 investments for which significant unobservable inputs were used to determine fair value:

| TOTAL INVESTMENTS | PREFERRED SECURITIES |
|-------------------|----------------------|
|                   | BANKING              |

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|  |           |           |
|--|-----------|-----------|
| BALANCE AS OF 11/30/09 .....                         | \$ 49,500 | \$ 49,500 |
| Accrued discounts/premiums .....                     | --        | --        |
| Realized gain/(loss) .....                           | --        | --        |
| Change in unrealized appreciation/(depreciation) ... | (14,760)  | (14,760)  |
| Net purchases/(sales) .....                          | --        | --        |
| Transfers in and/or out of Level 3 .....             | --        | --        |
|  | -----     | -----     |
| BALANCE AS OF 8/31/10 .....                          | \$ 34,740 | \$ 34,740 |

For the period ended August 31, 2010, total change in unrealized gain/(loss) on Level 3 securities still held at period-end and included in the change in net assets was \$(14,760).

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DIRECTORS

Donald F. Crumrine, CFA  
 Chairman of the Board  
 David Gale  
 Morgan Gust  
 Karen H. Hogan  
 Robert F. Wulf, CFA

OFFICERS

Donald F. Crumrine, CFA  
 Chief Executive Officer  
 Robert M. Ettinger, CFA  
 President  
 R. Eric Chadwick, CFA  
 Chief Financial Officer,  
 Vice President and Treasurer  
 Chad C. Conwell  
 Chief Compliance Officer,  
 Vice President and Secretary  
 Bradford S. Stone  
 Vice President and  
 Assistant Treasurer  
 Laurie C. Lodolo  
 Assistant Compliance Officer,  
 Assistant Treasurer and  
 Assistant Secretary  
 Linda M. Puchalski  
 Assistant Treasurer

INVESTMENT ADVISER

Flaherty & Crumrine Incorporated  
 e-mail: flaherty@pfdincome.com

QUESTIONS CONCERNING YOUR SHARES OF FLAHERTY & CRUMRINE PREFERRED INCOME FUND?

- If your shares are held in a Brokerage Account, contact your Broker.
- If you have physical possession of your shares in certificate form, contact the Fund's Transfer Agent & Shareholder Servicing Agent --

BNY Mellon Investment Servicing (US) Inc.  
P.O. Box 43027  
Providence, RI 02940-3027  
1-800-331-1710

THIS REPORT IS SENT TO SHAREHOLDERS OF FLAHERTY & CRUMRINE PREFERRED INCOME FUND INCORPORATED FOR THEIR INFORMATION. IT IS NOT A PROSPECTUS, CIRCULAR OR REPRESENTATION INTENDED FOR USE IN THE PURCHASE OR SALE OF SHARES OF THE FUND OR OF ANY SECURITIES MENTIONED IN THIS REPORT.

(FLAHERTY & CRUMRINE LOGO)  
PREFERRED INCOME FUND

Quarterly  
Report

August 31, 2010

[www.preferredincome.com](http://www.preferredincome.com)