

FLAHERTY & CRUMRINE PREFERRED INCOME FUND

To the Shareholders of Flaherty & Crumrine Preferred Income Fund:

The new fiscal year began much like the previous year ended. For the three month period ended February 28, 2010, total return (principal change and income) on net asset value of the Fund was +10.9%. Over the same period, total return on market price of Fund shares was +27.2%.

The strong performance came as credit markets continued to recover from the depths of the financial crisis last year. Economists and investors have expressed confidence that our financial system is back on track, and, although problems persist, seeds of recovery are in place. We share this view and encourage you to visit www.preferredincome.com to read our Quarterly Economic Update.

Over the past several quarters, the focus of these letters has been the financial crisis and its impact on the Fund's investment portfolio. We experienced gut-wrenching market weakness starting in the second half of 2008 and continuing into early 2009, only to watch prices rebound dramatically in the months since. Never before have we seen such extreme volatility over a relatively short time frame. We expect smoother waters ahead, but, as always, the future will be filled with challenges and opportunities.

We will take advantage of this relative calm to review the market for preferred securities a bit more broadly than our typical quarterly letter. After turbulence, the time seems right to take a step back and regain some perspective on the market. Readers can compare these broad market comments to the Fund's investments summarized on the following pages.

As of February 28, 2010, the market for preferred securities has grown to \$378 billion¹ from \$231 billion in 2005. The issues that comprise the market are far from homogeneous. An issuer is now able to tailor a preferred security to its specific financing needs by choosing from a wide range of features. Because of the variety of terms preferreds have, it has become easier to define a preferred by what it is not—a preferred security is not senior debt and it is not common stock.

Fifteen percent of the market is “traditional” preferred, i.e. the distributions to investors are *dividends*, and paid from after-tax income of the issuer. These distributions may have after-tax benefits to investors. 85% is “taxable” preferred that pay *interest*²; these payments are treated as interest expense for issuers and ordinary income for investors.

Many features of preferred securities are especially beneficial to companies in highly-regulated industries. Preferred issues from utilities, banks and insurance companies comprise over 80% of the preferred market. Of course, as the experience of the past couple of years serves to remind us, regulators can contribute to problems at the companies they regulate. Nonetheless, regulators recognize the critical role of the preferred market, and have helped facilitate growth in the asset class.

Despite a rash of downgrades during the financial crisis, the market is still comprised of mostly investment-grade issues. 64% of preferred issues are rated Baa or higher. A substantially larger portion of the preferred universe is comprised of issuers with *senior debt* rated investment grade. For this reason, preferred securities are widely considered to be the highest yielding asset class of investment grade companies.

¹ Market statistics used in this report, along with a wide range of additional information can be viewed by visiting the Flaherty & Crumrine website, www.preferredstockguide.com.

² We include preferred securities issued in the United States by foreign domiciled entities in the “taxable” category; many of these issues make distributions considered to be dividends for some types of investors

A word about credit analysis is in order. We have always based investment decisions on our internal credit research, and try to own credits that we believe are investment grade quality. Of course, credit analysis is more art than science, and no one does it perfectly, but we think our team does an outstanding job.

Our focus is first and foremost on preferred securities. The objective of our credit analysis is to develop an in-depth opinion about the quality of each security in the Fund. This approach differs from the rating agencies, where the focus is primarily on the quality of an issuer's most senior debt. Once the senior debt rating is determined, a mechanical "notching" methodology is applied to rate subordinated classes of securities, such as the issuer's preferreds (rating agency methodology brings to mind the Bismarck quote, "laws are like sausages, it is better not to see them being made").

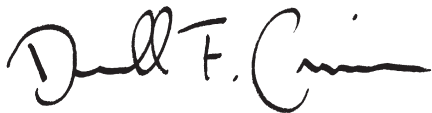
Much has been made recently about potential conflicts at the public rating agencies. Whether the conflicts are real or perceived, the business model of the agencies is likely to change. Regardless of how one views the public rating agencies, we don't face those conflicts and care only about choosing the right investments for the Fund. We pay close attention to the public ratings, but our investment decisions are only made after we do our own homework.

One additional question that should be on the minds of shareholders: can the Fund continue to produce double-digit quarterly returns? The answer shouldn't be surprising—it's not likely. By a variety of measures, in our view, the preferred market remains attractive relative to other asset classes. But the disparity is not as glaring as it was last spring and, in fact, is now approaching a range we consider normal.

Of course, preferred security prices never experienced anything like the volatility they experienced during the recent financial crisis. Historically, investors have (quite properly) owned these securities for the income they produce; only recently have they attracted the attention of those more inclined toward casinos. Now that the economy is beginning to stabilize, the wrath of recent markets seems to have instilled a new sense of discipline and propriety on companies that lost their way. Nonetheless, we will continue to keep a close eye on how those companies adapt to this new environment.

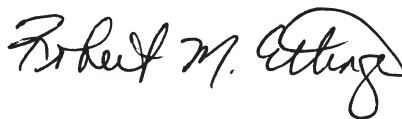
More information is always available on the Fund's website at www.preferredincome.com.

Sincerely,



Donald F. Crumrine
Chairman of the Board

April 21, 2010



Robert M. Ettinger
President

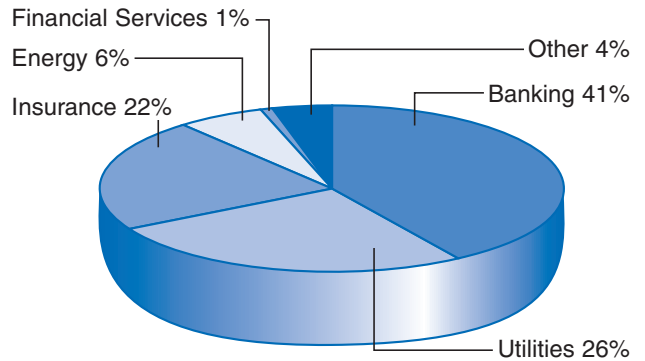
PORTFOLIO OVERVIEW
February 28, 2010 (Unaudited)

Fund Statistics

Net Asset Value	\$	10.67
Market Price	\$	11.37
Premium		6.56%
Yield on Market Price		7.60%
Common Stock Shares Outstanding		10,685,849

Industry Categories

% of Net Assets†



Moody's Ratings

% of Net Assets†

AA	0.3%
A	8.6%
BBB	67.5%
BB	19.6%
Below "BB"	0.6%
Not Rated	1.2%
Below Investment Grade*	15.2%

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

Top 10 Holdings by Issuer

% of Net Assets†

Banco Santander	6.8%
PNC Financial Services	5.7%
Capital One Financial	4.4%
Liberty Mutual Group	4.1%
Metlife	3.8%
Dominion Resources	3.7%
Comerica	3.5%
Goldman Sachs	3.3%
Interstate Power & Light	2.9%
HSBC Plc	2.8%

% of Net Assets†**

Holdings Generating Qualified Dividend Income (QDI) for Individuals	43%
Holdings Generating Income Eligible for the Corporate Dividends Received Deduction (DRD)	29%

** 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.

PORTFOLIO OF INVESTMENTS

February 28, 2010 (Unaudited)

Shares/\$ Par	Value
Preferred Securities — 95.0%	
Banking — 41.3%	
\$ 2,750,000	Astoria Capital Trust I, 9.75% 11/01/29, Series B \$ 2,861,625 ⁽¹⁾
417,300	Banco Santander, 10.50% Pfd., Series 10 11,493,485 ^{** (1)(2)}
48,700	Bank of America Corporation, 6.70% Pfd. 1,079,192 ^{* (1)}
	Barclays Bank PLC:
\$ 3,250,000	6.278% 2,486,250 ⁽¹⁾⁽²⁾
40,000	6.625% Pfd., Series 2 863,600 ^{* (1)(2)}
20,000	8.125% Pfd., Series 5 502,000 ^{** (2)}
87,500	BB&T Capital Trust VI, 9.60% Pfd. 2,493,750 ⁽¹⁾
\$ 5,100,000	Capital One Capital III, 7.686% 08/15/36 4,799,100 ⁽¹⁾
\$ 2,500,000	Capital One Capital VI, 8.875% 05/15/40 2,671,040
\$ 5,210,000	Colonial BancGroup, 7.114%, 144A**** 15,630 ^{††}
\$ 7,100,000	Comerica Capital Trust II, 6.576% 02/20/37 5,946,250 ⁽¹⁾
9,000	FBOP Corporation, Adj. Rate Pfd., 144A**** 61,740 ^{*††}
1,250	First Republic Preferred Capital Corporation, 10.50% Pfd., 144A**** 1,162,500 ⁽¹⁾
22,500	First Republic Preferred Capital Corporation II, 8.75% Pfd., Series B, 144A**** 561,094 ⁽¹⁾
3,250	First Tennessee Bank, Adj. Rate Pfd., 144A**** 1,851,484 ^{* (1)}
\$ 600,000	First Tennessee Capital I, 8.07% 01/06/27, Series A 532,874
\$ 500,000	First Tennessee Capital II, 6.30% 04/15/34, Series B 352,891
\$ 1,500,000	First Union Capital II, 7.95% 11/15/29 1,542,829 ⁽¹⁾
	Goldman Sachs:
\$ 5,040,000	Capital II, 5.793% 4,044,600 ⁽¹⁾
2,500	STRIPES Custodial Receipts, Pvt. 1,525,000 [*]
\$ 500,000	HSBC USA Capital Trust II, 8.38% 05/15/27, 144A**** 478,731
	HSBC USA, Inc.:
46,200	Adj. Rate Pfd., Series D 1,076,576 ^{* (1)}
109,700	6.50% Pfd., Series H 2,667,081 ^{* (1)}
4,400	\$2.8575 Pfd. 194,260 ^{* (1)}
\$ 950,000	JPMorgan Chase Capital XXVII, 7.00% 11/01/39, Series AA 968,468
15,000	JPMorgan Chase Capital XXVIII, 7.20% Pfd. 12/22/39 395,157
15,000	Keycorp Capital VIII, 7.00% Pfd. 06/15/66 334,688 ⁽¹⁾
23,500	Keycorp Capital X, 8.00% Pfd. 587,265 ⁽¹⁾
\$ 550,000	Lloyds Banking Group PLC, 6.657%, 144A**** 294,250 ^{** (2)†}
25,000	Morgan Stanley Capital Trust VIII, 6.45% Pfd. 04/15/67 546,750
31,500	PFGI Capital Corporation, 7.75% Pfd. 720,563 ⁽¹⁾
250,300	PNC Financial Services, 9.875% Pfd., Series F 7,336,919 ^{* (1)}
\$ 1,600,000	PNC Preferred Funding Trust III, 8.70%, 144A**** 1,677,274 ⁽¹⁾
1,750	Sovereign REIT, 12.00% Pfd., Series A, 144A**** 1,999,375

PORTFOLIO OF INVESTMENTS (Continued)

February 28, 2010 (Unaudited)

<u>Shares/\$ Par</u>		<u>Value</u>
Preferred Securities — (Continued)		
Banking — (Continued)		
\$ 2,400,000	Wachovia Capital Trust III, 5.80%	\$ 1,956,000
\$ 1,000,000	Washington Mutual, 9.75%, 144A****	32,500††
\$ 1,600,000	Webster Capital Trust IV, 7.65% 06/15/37	1,040,000 ⁽¹⁾
\$ 1,000,000	Wells Fargo Capital XV, 9.75%	1,090,700
		<u>70,243,491</u>
Financial Services — 0.5%		
\$ 500,000	General Electric Capital Corporation, 6.375% 11/15/67	448,125
15,300	HSBC Finance Corporation, 6.36% Pfd.	354,769*
	Lehman Brothers Holdings, Inc.:	
15,000	5.67% Pfd., Series D	7,125*††
19,500	5.94% Pfd., Series C	8,775*††
25,000	6.50% Pfd., Series F	3,813*††
27,500	7.95% Pfd.	3,768*††
		<u>826,375</u>
Insurance — 19.5%		
\$ 1,000,000	Ace Capital Trust II, 9.70% 04/01/30	1,162,374 ⁽¹⁾⁽²⁾
22,800	Arch Capital Group Ltd., 8.00% Pfd., Series A	577,125** ⁽¹⁾⁽²⁾
	AXA SA:	
\$ 1,500,000	6.379%, 144A****	1,211,250** ⁽¹⁾⁽²⁾
\$ 3,000,000	6.463%, 144A****	2,392,500** ⁽¹⁾⁽²⁾
35,900	Axis Capital Holdings, 7.50% Pfd., Series B	3,073,937 ⁽¹⁾⁽²⁾
90,600	Delphi Financial Group, 7.376% Pfd. 05/15/37	1,817,662 ⁽¹⁾
\$ 3,540,000	Everest Re Holdings, 6.60% 05/15/37	2,849,700 ⁽¹⁾
	Liberty Mutual Group:	
\$ 800,000	7.80% 03/15/37, 144A****	692,000 ⁽¹⁾
\$ 4,000,000	10.75% 06/15/58, 144A****	4,360,000 ⁽¹⁾
\$ 500,000	MetLife Capital Trust IV, 7.875% 12/15/37, 144A****	495,000 ⁽¹⁾
\$ 2,000,000	MetLife Capital Trust X, 9.25% 04/08/38, 144A****	2,240,000 ⁽¹⁾
	MetLife, Inc.:	
89,400	6.50% Pfd., Series B	2,209,298* ⁽¹⁾
\$ 1,250,000	10.75% 08/01/39	1,544,152 ⁽¹⁾
	Principal Financial Group:	
5,000	5.563% Pfd., Series A	411,250*
100,000	6.518% Pfd., Series B	2,261,250* ⁽¹⁾
	Renaissancere Holdings Ltd.:	
122,250	6.08% Pfd., Series C	2,518,350** ⁽¹⁾⁽²⁾

PORTFOLIO OF INVESTMENTS (Continued)

February 28, 2010 (Unaudited)

<u>Shares/\$ Par</u>	<u>Value</u>
Preferred Securities — (Continued)	
Insurance — (Continued)	
6,900 6.60% Pfd., Series D	\$ 149,454** ⁽²⁾
9,200 7.30% Pfd., Series B	224,963** ⁽²⁾
119,500 Scottish Re Group Ltd., 7.25% Pfd.	700,569** ⁽²⁾ †
\$ 750,000 USF&G Capital, 8.312% 07/01/46, 144A****	776,964 ⁽¹⁾
\$ 2,000,000 XL Capital Ltd., 6.50%, Series E	1,587,600 ⁽¹⁾⁽²⁾
	33,255,398
Utilities — 25.9%	
10,000 Baltimore Gas & Electric Company, 6.70% Pfd., Series 1993	977,813 ⁽¹⁾
\$ 2,491,000 COMED Financing III, 6.35% 03/15/33	2,038,042 ⁽¹⁾
\$ 250,000 Dominion Resources Capital Trust I, 7.83% 12/01/27	258,849
\$ 3,500,000 Dominion Resources, Inc.: 7.50%	3,469,329 ⁽¹⁾
90,000 8.375% Pfd., Series A	2,560,500 ⁽¹⁾
40,000 Entergy Arkansas, Inc., 6.45% Pfd.	891,252* ⁽¹⁾
\$ 2,000,000 FPL Group Capital, Inc., 6.65% 06/15/67	1,862,612
Georgia Power Company: 12,600 6.125% Pfd.	316,543* ⁽¹⁾
12,500 6.50% Pfd., Series 2007A	1,264,844* ⁽¹⁾
3,000 Gulf Power Company, 6.45% Pfd., Series 2007A	296,815* ⁽¹⁾
32,650 Indianapolis Power & Light Company, 5.65% Pfd.	2,831,369*
170,900 Interstate Power & Light Company, 8.375% Pfd., Series B	4,966,781* ⁽¹⁾
Pacific Enterprises: 22,430 \$4.50 Pfd.	1,762,157* ⁽¹⁾
10,000 \$4.75 Pfd., Series 53	830,800* ⁽¹⁾
\$ 500,000 PECO Energy Capital Trust III, 7.38% 04/06/28, Series D	470,343 ⁽¹⁾
\$ 4,400,000 Puget Sound Energy, Inc., 6.974% 06/01/67	3,921,051 ⁽¹⁾
60,000 Scana Corporation, 7.70% Pfd.	1,622,400 ⁽¹⁾
Southern California Edison: 35,000 6.00% Pfd., Series C	3,189,375* ⁽¹⁾
11,500 6.125% Pfd.	1,075,610* ⁽¹⁾
\$ 3,000,000 Southern Union Company, 7.20% 11/01/66	2,707,500 ⁽¹⁾
\$ 750,000 TXU Electric Capital V, 8.175% 01/30/37	228,750
18,800 Union Electric Company, \$7.64 Pfd.	1,883,525* ⁽¹⁾

PORTFOLIO OF INVESTMENTS (Continued)

February 28, 2010 (Unaudited)

<u>Shares/\$ Par</u>		<u>Value</u>
Preferred Securities — (Continued)		
Utilities — (Continued)		
\$ 3,900,000	Wisconsin Energy Corporation, 6.25% 05/15/67	\$ 3,602,843 ⁽¹⁾
14,750	Xcel Energy, Inc., \$4.08 Pfd., Series B	1,076,013*
		<u>44,105,116</u>
Energy — 6.1%		
\$ 4,700,000	Enbridge Energy Partners LP, 8.05% 10/01/37	4,647,821 ⁽¹⁾
	Enterprise Products Partners:	
\$ 750,000	7.00% 06/01/67	680,930
\$ 1,500,000	8.375% 08/01/66, Series A	1,518,735 ⁽¹⁾
3,500	Kinder Morgan GP, Inc., 8.33% Pfd., 144A****	3,503,500*
		<u>10,350,986</u>
Miscellaneous Industries — 1.7%		
40,000	Ocean Spray Cranberries, Inc., 6.25% Pfd., 144A****	2,903,752 ⁽¹⁾
		<u>2,903,752</u>
Total Preferred Securities		
	(Cost \$161,811,457)	<u>161,685,118</u>
Corporate Debt Securities — 2.7%		
Financial Services — 0.1%		
10,000	Ameriprise Financial, Inc., 7.75% 06/15/39	259,225 ⁽¹⁾
		<u>259,225</u>
Insurance — 2.3%		
\$ 2,200,000	Liberty Mutual Insurance, 7.697% 10/15/97, 144A****	1,933,961 ⁽¹⁾
\$ 2,000,000	UnumProvident Corporation, 7.25% 03/15/28, Senior Notes	1,902,702 ⁽¹⁾
		<u>3,836,663</u>
Utilities — 0.3%		
20,000	Entergy Texas, Inc., 7.875% 06/01/39	567,000
		<u>567,000</u>
Total Corporate Debt Securities		
	(Cost \$3,944,512)	<u>4,662,888</u>

PORTFOLIO OF INVESTMENTS (Continued)

February 28, 2010 (Unaudited)

<u>Shares/\$ Par</u>	<u>Value</u>
Common Stock — 0.1%	
Banking — 0.1%	
3,620 CIT Group, Inc.	\$ 131,877*†
Total Common Stock	
(Cost \$330,325)	
	131,877
Money Market Fund — 1.7%	
2,855,270 BlackRock Provident Institutional, T-Fund	2,855,270
Total Money Market Fund	
(Cost \$2,855,270)	
	2,855,270
Total Investments (Cost \$168,941,564***)	99.5% 169,335,153
Other Assets And Liabilities (Net)	0.5% 778,957
Net Assets before loan	100.0%‡ \$ 170,114,110
Loan Principal Balance	(56,100,000)
Total Net Assets Available To Common Stock	\$ 114,014,110

* 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 February 28, 2010, these securities amounted to \$28,643,505 or 16.8% of net assets before loan. These securities have been determined to be liquid under the guidelines established by the Board of Directors.

(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 \$125,486,320 at February 28, 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

REIT — Real Estate Investment Trust

STRIPES — Structured Residual Interest Preferred Enhanced Securities

STATEMENT OF CHANGES IN NET ASSETS AVAILABLE TO COMMON STOCK⁽¹⁾
For the period from December 1, 2009 through February 28, 2010 (Unaudited)

	<u>Value</u>
OPERATIONS:	
Net investment income	\$ 2,750,803
Net realized gain/(loss) on investments sold during the period	(1,565,597)
Change in net unrealized appreciation/depreciation of investments	10,290,524
Distributions to APS* Shareholders from net investment income, including changes in accumulated undeclared distributions	<u>(70,977)</u>
Net increase in net assets resulting from operations	11,404,753
DISTRIBUTIONS:	
Dividends paid from net investment income to Common Stock Shareholders ⁽²⁾	<u>(2,306,539)</u>
Total Distributions to Common Stock Shareholders	(2,306,539)
FUND SHARE TRANSACTIONS:	
Increase from shares issued under the Dividend Reinvestment and Cash Purchase Plan	<u>151,775</u>
Net increase in net assets available to Common Stock resulting from Fund share transactions	151,775
NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD	<u>\$ 9,249,989</u>

NET ASSETS AVAILABLE TO COMMON STOCK:

Beginning of period	\$ 104,764,121
Net increase in net assets during the period	<u>9,249,989</u>
End of period	<u>\$ 114,014,110</u>

* Auction Preferred Stock.

⁽¹⁾ These tables summarize the three months ended February 28, 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.

FINANCIAL HIGHLIGHTS⁽¹⁾

For the period from December 1, 2009 through February 28, 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 0.26

Net realized and unrealized gain/(loss) on investments 0.82

DISTRIBUTIONS TO APS* SHAREHOLDERS:

From net investment income (0.01)

Total from investment operations 1.07

DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS:

From net investment income (0.22)

Total distributions to Common Stock Shareholders (0.22)

Net asset value, end of period \$ 10.67

Market value, end of period \$ 11.37

Common Stock shares outstanding, end of period 10,685,849

RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:

Net investment income† 10.07%**

Net investment income, including payments to APS Shareholders† 9.81%**

Operating expenses including interest expense 2.33%**

Operating expenses excluding interest expense 1.67%**

SUPPLEMENTAL DATA:††

Portfolio turnover rate 4%***

Net assets before loan, end of period (in 000's) \$ 170,114

Ratio of operating expenses including interest expense⁽²⁾ to net assets before loan and APS 1.57%**

Ratio of operating expenses excluding interest expense⁽²⁾ to net assets before loan and APS 1.13%**

⁽¹⁾ These tables summarize the three months ended February 28, 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.

FINANCIAL HIGHLIGHTS (Continued)
Per Share of Common Stock (Unaudited)

	<u>Total Dividends Paid</u>	<u>Net Asset Value</u>	<u>NYSE Closing Price</u>	<u>Dividend Reinvestment Price⁽¹⁾</u>
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

⁽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.

NOTES TO FINANCIAL STATEMENTS (Unaudited)

1. Aggregate Information for Federal Income Tax Purposes

At February 28, 2010 the aggregate cost of securities for federal income tax purposes was \$168,938,993, the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was \$23,247,156 and the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was \$22,850,996.

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)

The inputs or methodology used for valuing securities are not necessarily an indication of the risk associated with investing in those securities. A summary of the inputs used to value the Fund's net assets as of February 28, 2010 is as follows:

	<u>Total Value at February 28, 2010</u>	<u>Level 1 Quoted Price</u>	<u>Level 2 Significant Observable Inputs</u>	<u>Level 3 Significant Unobservable Inputs</u>
Preferred Securities				
Banking	\$70,243,491	\$46,919,881	\$23,261,870	\$ 61,740
Financial Services	826,375	802,894	23,481	—
Insurance	33,255,398	14,737,823	18,517,575	—
Utilities	44,105,116	12,935,553	31,169,563	—
Energy	10,350,986	—	10,350,986	—
Miscellaneous Industries	2,903,752	—	2,903,752	—
Corporate Debt Securities	4,662,888	826,225	3,836,663	—
Common Stock				
Banking	131,877	131,877	—	—
Money Market Fund	2,855,270	2,855,270	—	—
Total Investments	<u>\$169,335,153</u>	<u>\$79,209,523</u>	<u>\$90,063,890</u>	<u>\$ 61,740</u>

NOTES TO FINANCIAL STATEMENTS (Unaudited) (Continued)

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

	<u>Preferred Securities</u>	
	Total Investments	Banking
Balance as of 11/30/09	\$ 49,500	\$ 49,500
Accrued discounts/premiums	—	—
Realized gain/(loss)	—	—
Change in unrealized appreciation/(depreciation)	12,240	12,240
Net purchases/(sales)	—	—
Transfers in and/or out of Level 3	—	—
Balance as of 2/28/10	\$ 61,740	\$ 61,740

For the period ended February 28, 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 \$12,240.

[This page intentionally left blank]

[This page intentionally left blank]

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

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 —
PNC Global Investment Servicing
(U.S.) 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

PREFERRED INCOME FUND

Quarterly Report

February 28, 2010

www.preferredincome.com