

FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC

Form N-30B-2

October 23, 2007

FLAHERTY & CRUMRINE PREFERRED INCOME FUND

To the Shareholders of the Flaherty & Crumrine Preferred Income Fund ("PFD"):

Beginning with issues arising in the subprime mortgage loan market, a well-publicized series of events has roiled financial markets over the past several months. The preferred stock market and closed-end funds have been particularly impacted, and, consequently, for the Fund's third fiscal quarter ended August 31, 2007, the Fund had a total return of -4.9% on the net asset value (NAV) of its Common Stock.

As we've discussed in prior letters, problems in the subprime mortgage loan market first bubbled up in January of this year. Throughout this year, the Fund has had no direct exposure to subprime loans, and we avoided investing in companies that had meaningful risks associated with the product. Our research team closely monitors the loan quality and underwriting standards of each financial company in the portfolio, and we invest only in companies that meet our quality thresholds. We're not perfect, but we believe that the Fund's portfolio is comprised of holdings in fundamentally sound companies.

In isolation, the impact of this weakness in the subprime loan market should have been limited to direct participants in this market; unfortunately, given the complexity of the financial system, few things happen in isolation. When the subprime problems became more pronounced several months ago, the fallout from this subprime weakness has been widespread and severe.

Fueled by low interest rates and relatively relaxed financing terms, a great deal more leverage had become built into the system than even just a few years ago. As investments directly associated with subprime mortgages declined significantly in value during the quarter, they became very illiquid. Highly-leveraged investors then were forced to sell other more liquid types of assets like investment-grade preferred and debt securities to meet redemptions or margin calls. Risk and liquidity premiums surged, indiscriminately taking yields on all credit instruments with them. In short, excess leverage created the financial powder keg and subprime loan problems provided the spark.

With yields on preferred securities rising more than yields on more senior debt securities, the prices of the securities in our portfolio fell as the supply of preferred securities exceeded demand. The rearview mirror is still a bit foggy, but it appears that much of the selling pressure came from hedge funds. Hedge funds had become the 800-pound gorilla in the credit markets recently, and although they've been forced to slim down, they can still have a big impact.

Hedge funds were not the only investors selling, but since they aren't required to disclose their preferred securities holdings, no one knows how extensive their selling pressure was. As a result, prospective buyers were extremely cautious because they feared additional selling would further depress prices. Wall Street brokers and dealers normally stand ready to provide liquidity to sellers, but they appeared reluctant to buy. Long-term investors like the Fund, as well as individual investors, insurance companies and pension funds, also stayed on the sidelines for the most part. During the quarter, and since it ended, we have added some positions at attractive levels, but we are continuing to take a go-slow approach.

Subprime fallout also extended to the market for short-term, or money-market, securities such as commercial paper and auction-rate securities. This market was in a state of disarray throughout August and into early September. Investors in money-market securities don't like risk, and, at the

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slightest hint of trouble, they pull their money out and invest in short-term government securities. While the perception of risk is real for a small segment of borrowers, the reaction seems to be disproportionate.

These disruptions in the short-term market impacted the Fund in two meaningful ways. First, they contributed to price weakness in many of the Fund's investments, particularly in financial companies.

While banks can fulfill their short-term financing needs with customer deposits and through the Federal Reserve, finance companies like broker-dealers need to rely on the short-term securities market to run their day-to-day operations. This market is like oxygen to most financial companies, and restricting their borrowing makes it more expensive for them to operate. We continue to believe that none of the financial companies in our portfolio face significant risks of default as a result of this increased cost of borrowing, but it has clearly impacted their earnings outlooks and the prices of their preferred securities.

Second, the rates paid by the Fund on its own auction-rate Preferred Stock have risen significantly as a direct result of liquidity problems in the financial markets. The frustrating irony is that the Fund's own Preferred Stock is of very high quality with a rating of AA and logic would dictate that rates should fall as investors seek out higher quality investments. This high quality is a function of the Investment Company Act (which governs the Fund) and the guidelines imposed by the rating agencies. As Kevin Conery, Merrill Lynch's Preferred Stock Strategist, recently observed about the Investment Company Act, "while some have criticized it for being too conservative for its 200% asset coverage test, at times like these in the market, we respect this discipline." While we are beginning to see some improvement in the auction rates of our Preferred Stock, and the recent interest rate cut by the Federal Reserve should help over the coming months, we haven't yet returned to more normalized auction rates.

The higher cost of our auction-rate Preferred Stock comes directly out of money available for distribution as the monthly Common Stock dividend. On the plus side, higher yields on preferred stock mean that we have been able to increase the income earned on the portfolio. It will take some time to see how these two offsetting factors affect income; in the meantime we are doing our best to manage both. We are comfortable with the current dividend, but we strive to pay out a rate that is sustainable and will make adjustments as conditions warrant.

We have been through periods of fear and volatility before, and we remain optimistic about long-term prospects for the Fund. Such periods create opportunities to buy securities of sound companies at discounted prices, as many shorter-term investors exit the market by selling both good and bad investments. We expect both more rational pricing and reduced risk of early redemption of our portfolio securities as markets settle down - both of which should benefit future returns for long-term investors. In addition, our Preferred Stock auction rates are likely to normalize in due course, as the market begins to better recognize the credit quality of our Preferred Stock. While we cannot say with certainty when, or if, these things will happen, as managers we are doing our best to position the Fund to ride out the current storm and prepare for better days ahead.

In volatile market conditions like these, we may provide more frequent updates about the preferred securities market and the Fund's portfolio. We did so this past quarter by adding special Questions and Answers regarding the market price of the Fund's shares to the Fund's website at [WWW.PREFERREDINCOME.COM](http://WWW.PREFERREDINCOME.COM). We encourage you to stay informed as shareholders by periodically visiting the website for additional information about your Fund.

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Sincerely,

/s/ Donald F. Crumrine

/s/ Robert M. Ettinger

Donald F. Crumrine  
Chairman of the Board

Robert M. Ettinger  
President

October 17, 2007

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 Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OVERVIEW  
 AUGUST 31, 2007 (UNAUDITED)  
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FUND STATISTICS ON 08/31/07

|                                 |    |            |
|---------------------------------|----|------------|
| Net Asset Value                 | \$ | 14.19      |
| Market Price                    | \$ | 14.13      |
| Discount                        |    | 0.42%      |
| Yield on Market Price           |    | 7.30%      |
| Common Stock Shares Outstanding |    | 10,530,560 |

| MOODY'S RATINGS         | % OF PORTFOLIO |
|-------------------------|----------------|
| AA                      | 6.5%           |
| A                       | 15.8%          |
| BBB                     | 51.9%          |
| BB                      | 13.2%          |
| Not Rated               | 10.5%          |
| Below Investment Grade* | 16.1%          |

\* BELOW INVESTMENT GRADE BY BOTH MOODY'S AND S&P.

[THE FOLLOWING TABLE WAS REPRESENTED BY A PIE CHART IN THE PRINTED MATERIAL.]

| INDUSTRY CATEGORIES | % OF PORTFOLIO |
|---------------------|----------------|
| Utilities           | 32%            |
| Banking             | 30%            |
| Insurance           | 15%            |
| Financial Services  | 12%            |
| Energy              | 7%             |
| REITs               | 2%             |
| Other               | 2%             |

| TOP 10 HOLDINGS BY ISSUER | % OF PORTFOLIO |
|---------------------------|----------------|
| Interstate Power & Light  | 5.1%           |
| FBOP Corp                 | 4.0%           |
| Banco Santander           | 3.8%           |
| Liberty Mutual Group      | 3.7%           |
| First Republic Bank       | 3.6%           |
| Xcel Energy               | 3.1%           |
| SLM Corp                  | 3.1%           |
| CoBank ACB                | 2.9%           |
| EOG Resources             | 2.8%           |

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Goldman Sachs 2.3%

% OF PORTFOLIO\*\*

|   |     |
|---|-----|
| Holdings Generating Qualified Dividend Income (QDI) for Individuals                     | 61% |
| Holdings Generating Income Eligible for the Corporate Dividend Received Deduction (DRD) | 53% |

\*\* 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.

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS  
 AUGUST 31, 2007 (UNAUDITED)

SHARES/\$ PAR

PREFERRED SECURITIES -- 94.4%  
 BANKING -- 29.8%

|              |   |
|--------------|---|
| \$ 3,000,000 | Astoria Capital Trust I, 9.75% 11/01/29, Series B                               |
| 34,860       | BAC Capital Trust I, 7.00% Pfd. 12/15/31  |
| 7,700        | BAC Capital Trust II, 7.00% Pfd. 02/01/32                                       |
|              | Banco Santander:  |
| 25,000       | Adj. Rate Pfd., 144A****  |
| 301,200      | 6.50% Pfd., 144A****  |
| 63,200       | 6.80% Pfd., 144A****  |
| \$ 2,000,000 | Capital One Capital III, 7.686% 08/15/36  |
| \$ 3,500,000 | CBG Florida REIT Corporation, 7.114%, 144A****                                  |
| 19,648       | Citizens Funding Trust I, 7.50% Pfd. 09/15/66                                   |
|              | Cobank, ACB:  |
| 50,000       | 7.00% Pfd., 144A****  |
| 75,000       | 7.814% Pfd., 144A****   |
| \$ 2,575,000 | Comerica Capital Trust II, 6.576% 02/20/37                                      |
| 9,000        | FBOP Corporation, Adj. Rate Pfd., 144A****                                      |
| \$ 2,250,000 | First Hawaiian Capital I, 8.343% 07/01/27, Series B                             |
|              | First Republic Bank:  |
| 200,000      | 6.25% Pfd.  |
| 53,700       | 6.70% Pfd.  |
| 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**** |
| \$ 1,500,000 | Fleet Union Capital II, 7.95% 11/15/29  |
| 5,000        | Fleet Capital Trust VIII, 7.20% Pfd. 03/15/32                                   |
| 5,000        | HSBC Series II, Variable Inverse Pfd., Pvt.                                     |
| 2,500        | HSBC USA, Inc., \$2.8575 Pfd.   |
| 10,000       | ING Groep NV., 7.05% Pfd.   |
| 120,000      | Keycorp Capital IX, 6.75% Pfd. 12/15/66   |
| \$ 674,000   | NB Capital Trust II, 7.83% 12/15/26   |

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|    |           |  |
|----|-----------|--|
|    | 31,500    | PFGI Capital Corporation, 7.75% Pfd. ....                |
| \$ | 425,000   | Regions Financing Trust II, 6.625% 05/15/47 .....        |
|    | 10        | Roslyn Real Estate, 8.95% Pfd., Series C, 144A**** ..... |
|    | 77,600    | Sovereign Bancorp, 7.30% Pfd., Series C .....            |
|    | 30,600    | Sovereign Capital Trust V, 7.75% Pfd. 05/22/36 .....     |
| \$ | 1,000,000 | Sovereign Capital Trust VI, 7.908% 06/13/36 .....        |
|    |           | U.S. Bancorp, Auction Pass-Through Trust, Cl. B:         |
|    | 11        | Series 2006-5, Variable Rate Pfd., 144A**** .....        |
|    | 11        | Series 2006-6, Variable Rate Pfd., 144A**** .....        |
|    | 46,700    | USB Capital VIII, 6.35% Pfd. 12/29/65 .....              |
|    | 5,550     | Wachovia Capital Trust IX, 6.375% Pfd. ....              |

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 Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)  
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SHARES/\$ PAR  
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PREFERRED SECURITIES -- (CONTINUED)  
 BANKING -- (CONTINUED)

|    |           |  |
|----|-----------|--|
| \$ | 1,100,000 | Webster Capital Trust IV, 7.65% 06/15/37 .....   |
|    | 40,000    | Zions Capital Trust B, 8.00% Pfd. 09/01/32 ..... |

FINANCIAL SERVICES -- 11.1%

|    |           |  |
|----|-----------|--|
|    |           | CIT Group, Inc.:   |
| \$ | 2,600,000 | 6.10% .....  |
|    | 110,000   | 6.35% Pfd., Series A .....                                 |
|    | 25,000    | Countrywide Capital IV, 6.75% Pfd. ....                    |
|    | 50,300    | Countrywide Capital V, 7.00% Pfd. 11/01/36 .....           |
|    | 108,300   | Deutsche Bank Contingent Capital Trust II, 6.55% Pfd. .... |
|    |           | Goldman Sachs:   |
|    | 20,000    | Adj. Rate Pfd., Series A .....                             |
|    | 35,000    | Cabco Trust Capital I, Adj. Rate Pfd. 02/15/34 .....       |
|    | 25        | Pass-Through Certificates, Class B, 144A**** .....         |
|    | 2,500     | STRIPES Custodial Receipts, Pvt. ....                      |
|    |           | Merrill Lynch:   |
|    | 87,000    | Adj. Rate Pfd., Series 5 .....                             |
|    | 21,000    | Adj. Rate Pfd., Series H .....                             |
|    | 3,000     | Series II STRIPES Custodial Receipts, Pvt. ....            |
|    |           | SLM Corporation:   |
|    | 136,855   | 6.97% Pfd., Series A .....                                 |
|    | 9,000     | Adj. Rate Pfd., Series B .....                             |

INSURANCE -- 12.3%

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|    |           |  |
|----|-----------|--|
|    | 19,100    | ACE Ltd., 7.80% Pfd., Series C .....                     |
| \$ | 3,750,000 | AON Capital Trust A, 8.205% 01/01/27 .....               |
|    |           | Arch Capital Group Ltd.:                                 |
|    | 10,000    | 7.875% Pfd., Series B .....                              |
|    | 40,000    | 8.00% Pfd., Series A .....                               |
| \$ | 2,500,000 | AXA SA, 6.463%, 144A**** .....                           |
|    | 30,900    | Axis Capital Holdings, 7.50% Pfd., Series B .....        |
|    | 27,000    | Berkley W.R. Capital Trust II, 6.75% Pfd. 07/26/45 ..... |
|    | 75,000    | Delphi Financial Group, 7.376% Pfd. 05/15/37 .....       |
|    | 6,250     | Everest Re Capital Trust II, 6.20% Pfd., Series B .....  |
| \$ | 1,040,000 | Everest Re Holdings, 6.60% 05/15/37 .....                |
| \$ | 4,500,000 | Liberty Mutual Group, 7.80% 03/15/37, 144A**** .....     |
|    | 40,000    | MetLife, Inc., Adj. Rate Pfd., Series A .....            |

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)

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SHARES/\$ PAR

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

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|    |           |  |
|----|-----------|--|
| \$ | 1,650,000 | Progressive Corporation, Variable Rate, 06/15/37 ..... |
| \$ | 357,000   | Provident Financing Trust I, 7.405% 03/15/38 .....     |
|    |           | Renaissancere Holdings Ltd.:                           |
|    | 27,950    | 6.08% Pfd., Series C .....                             |
|    | 79,100    | 6.60% Pfd., Series D .....                             |
|    | 119,500   | Scottish Re Group Ltd., 7.25% Pfd. ....                |
| \$ | 750,000   | USF&G Capital, 8.312% 07/01/46, 144A**** .....         |
| \$ | 1,600,000 | XL Capital Ltd., 6.50%, Series E .....                 |

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UTILITIES -- 30.7%

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|  |         |  |
|--|---------|--|
|  |         | Alabama Power Company:   |
|  | 300     | 4.52% Pfd. ....  |
|  | 5,734   | 4.72% Pfd. ....  |
|  | 10,000  | Baltimore Gas & Electric Company, 6.70% Pfd., Series 1993 .....                |
|  | 103,200 | Calenergy Capital Trust III, 6.50% Pfd. 09/01/27 .....                         |
|  |         | Central Hudson Gas & Electric Corporation:                                     |
|  | 5,000   | 4.35% Pfd., Series D, Pvt. ....  |
|  | 900     | 4.96% Pfd., Series E, Pvt. ....  |
|  | 8,340   | Central Vermont Public Service Corporation, 8.30% Sinking Fund Pfd., Pvt. .... |
|  |         | Connecticut Light & Power Company:   |
|  | 12,124  | 4.50% Pfd., Series 1963, Pvt. ....   |
|  | 34,300  | 5.28% Pfd., Series 1967 .....  |
|  | 1,905   | 6.56% Pfd., Series 1968 .....  |
|  | 15,778  | \$3.24 Pfd. ....   |

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|         |   |
|---------|---|
| 2,100   | Consolidated Edison Company of New York, 4.65% Pfd., Series C ..... |
| 2,886   | Dayton Power and Light Company, 3.90% Pfd., Series C .....          |
|         | Duquesne Light Company:   |
| 7,675   | 4.10% Pfd. ....   |
| 9,190   | 4.15% Pfd. ....   |
| 910     | 4.20% Pfd. ....   |
| 5,490   | \$2.10 Pfd., Series A .....   |
| 100,000 | Entergy Arkansas, Inc., 6.45% Pfd. ....                             |
| 4,555   | Entergy Gulf States, Inc., 7.56% Pfd. ....                          |
| 36,000  | Entergy Louisiana, Inc., 6.95% Pfd. ....                            |
| 5,000   | Entergy Mississippi, Inc., 4.92% Pfd. ....                          |
| 18,535  | Florida Power Company, 4.75% Pfd. ....                              |
| 48,300  | FPC Capital I, 7.10% Pfd., Series A .....                           |
| 40,000  | FPL Group Capital, Inc., 6.60% Pfd. 10/01/66, Series A .....        |

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 Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)  
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SHARES/\$ PAR  
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PREFERRED SECURITIES -- (CONTINUED)  
 UTILITIES -- (CONTINUED)

|            |   |
|------------|---|
| 13,100     | Georgia Power Capital Trust, 6.125% Pfd. ....                       |
| 2,010      | Great Plains Energy, Inc., 4.50% Pfd. ....                          |
| 50,000     | Hawaiian Electric Company, Inc., 5.25% Pfd., Series H, Pvt. ....    |
| 32,650     | Indianapolis Power & Light Company, 5.65% Pfd. ....                 |
| 384,000    | Interstate Power & Light Company, 8.375% Pfd., Series B .....       |
|            | Pacific Enterprises:  |
| 27,430     | \$4.50 Pfd. ....  |
| 10,000     | \$4.75 Pfd., Series 53 .....  |
|            | Pacific Gas & Electric Co.:   |
| 7,600      | 4.50% Pfd., Series H .....  |
| 41,500     | 5.00% Pfd., Series D .....  |
| 79,086     | 5.00% Pfd., Series E .....  |
|            | PacifiCorp:   |
| 1,095      | 5.40% Pfd. ....   |
| 1,225      | \$4.56 Pfd. ....  |
| 14,542     | \$4.72 Pfd. ....  |
| \$ 500,000 | PECO Energy Capital Trust III, 7.38% 04/06/28, Series D .....       |
| 5,000      | PPL Electric Utilities Corporation, 6.75% Pfd. ....                 |
| 10,000     | Public Service Company of New Mexico, 4.58% Pfd., Series 1965 ..... |
|            | San Diego Gas & Electric Company:                                   |
| 1,200      | 4.40% Pfd. ....   |
| 700        | 4.50% Pfd. ....   |
| 77,000     | \$1.70 Pfd. ....  |
|            | South Carolina Electric & Gas Company:                              |
| 24,924     | 5.125% Purchase Fund Pfd., Pvt. ....                                |
| 6,703      | 6.00% Purchase Fund Pfd., Pvt. ....                                 |
| 10,600     | Southern California Edison, 6.00% Pfd. ....                         |

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|    |           |  |
|----|-----------|--|
|    |           | Southern Union Company:                                  |
| \$ | 200,000   | 7.20% 11/01/66 .....                                     |
|    | 64,800    | 7.55% Pfd. ....  |
| \$ | 750,000   | TXU Electric Capital V, 8.175% 01/30/37 .....            |
|    |           | Union Electric Company:                                  |
|    | 14,150    | 4.56% Pfd. ....  |
|    | 18,800    | \$7.64 Pfd. ....   |
|    | 12,500    | Virginia Electric & Power Company, \$7.05 Pfd. ....      |
|    | 47,400    | Virginia Power Capital Trust, 7.375% Pfd. 07/30/42 ..... |
| \$ | 1,900,000 | Wisconsin Energy Corporation, 6.25% 05/15/67 .....       |
|    |           | Wisconsin Power & Light Company:                         |
|    | 1,220     | 4.50% Pfd. ....  |
|    | 546       | 4.80% Pfd. ....  |

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 Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)  
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SHARES/\$ PAR  
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PREFERRED SECURITIES -- (CONTINUED)  
 UTILITIES -- (CONTINUED)  
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|  |        |                             |
|--|--------|-----------------------------|
|  |        | Xcel Energy, Inc.:          |
|  | 16,030 | \$4.08 Pfd., Series B ..... |
|  | 26,200 | \$4.10 Pfd., Series C ..... |
|  | 22,000 | \$4.11 Pfd., Series D ..... |
|  | 17,750 | \$4.16 Pfd., Series E ..... |
|  | 10,000 | \$4.56 Pfd., Series G ..... |

ENERGY -- 5.8%

|    |           |  |
|----|-----------|--|
|    | 8,000     | Devon Energy Corporation, 6.49% Pfd., Series A ..... |
|    |           | Enterprise Products Partners:                        |
| \$ | 2,600,000 | 7.034% 01/15/68 .....                                |
| \$ | 1,500,000 | 8.375% 08/01/66 .....                                |
|    | 5,985     | EOG Resources, Inc., 7.195% Pfd., Series B .....     |
| \$ | 1,225,000 | KN Capital Trust III, 7.63% 04/15/28 .....           |
|    | 10,000    | Lasmo America Limited, 8.15% Pfd., 144A**** .....    |

REAL ESTATE INVESTMENT TRUST (REIT) -- 2.4%

|  |         |   |
|--|---------|---|
|  | 1,000   | Equity Residential Properties, 8.29% Pfd., Series K ..... |
|  | 30,000  | PS Business Parks, Inc., 7.375% Pfd., Series O .....      |
|  |         | Public Storage, Inc.:                                     |
|  | 146,370 | 6.45% Pfd., Series F .....                                |
|  | 63,200  | 6.625% Pfd., Series M .....                               |



MISCELLANEOUS INDUSTRIES -- 2.1%

|        |  |
|--------|--|
| 13,600 | E.I. Du Pont de Nemours and Company, \$4.50 Pfd., Series B ..... |
| 40,000 | Ocean Spray Cranberries, Inc., 6.25% Pfd., 144A**** .....        |

U.S. GOVERNMENT SECURITIES -- 0.2%

|        |                                   |
|--------|-----------------------------------|
| 20,000 | Freddie Mac, 5.66% Series W ..... |
|--------|-----------------------------------|

TOTAL PREFERRED SECURITIES

(Cost \$215,823,816) .....

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)

SHARES/\$ PAR

CORPORATE DEBT SECURITIES -- 4.9%

FINANCIAL SERVICES -- 0.7%

|              |  |
|--------------|--|
| \$ 1,800,000 | Lehman Brothers Holdings, 6.875% 07/17/37, Sub. Note ..... |
|--------------|--|

INSURANCE -- 2.4%

|              |   |
|--------------|---|
| \$ 900,000   | Farmers Exchange Capital, 7.20% 07/15/48, 144A**** .....  |
| \$ 4,729,000 | Liberty Mutual Insurance, 7.697% 10/15/97, 144A**** ..... |

UTILITIES -- 0.8%

|              |  |
|--------------|--|
| \$ 1,000,000 | Duke Capital Corporation, 8.00% 10/01/19, Senior Notes ..... |
| 5,000        | Entergy Louisiana LLC, 7.60% 04/01/32 .....                  |
| 20,100       | PPL Capital Funding, Inc., 6.85% 07/01/47 .....              |

ENERGY -- 1.0%

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\$ 2,450,000 KN Energy, Inc., 7.45% 03/01/98 .....  
 11,300 Nexen, Inc., 7.35% Subordinated Notes .....

TOTAL CORPORATE DEBT SECURITIES  
 (Cost \$11,443,348) .....

OPTION CONTRACTS -- 0.0%  
 515 December Put Options on December U.S. Treasury Bond Futures, Expiring 11/20/07 ...  
 1,025 October Put Options on December U.S. Treasury Bond Futures, Expiring 09/21/07 ....

TOTAL OPTION CONTRACTS  
 (Cost \$191,691) .....

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Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 AUGUST 31, 2007 (UNAUDITED)

SHARES/\$ PAR

MONEY MARKET FUND -- 0.1%  
 276,354 BlackRock Provident Institutional, TempFund .....

TOTAL MONEY MARKET FUND  
 (Cost \$276,354) .....

SECURITIES LENDING COLLATERAL -- 0.3%  
 573,900 Institutional Money Market Trust .....

TOTAL SECURITIES LENDING COLLATERAL  
 (Cost \$573,900) .....

TOTAL INVESTMENTS (Cost \$228,309,109\*\*\*) .....  
 OTHER ASSETS AND LIABILITIES (Net) .....

TOTAL NET ASSETS AVAILABLE TO COMMON AND PREFERRED STOCK .....

MONEY MARKET CUMULATIVE PREFERRED (TM) STOCK (MMP (R)) REDEMPTION VALUE .....

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.

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- \*\*\* 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. These securities have been determined to be liquid under the guidelines established by the Board of Directors.
- (1) Foreign Issuer.
- (2) Security on loan.
- + Non-income producing.
- ++ The percentage shown for each investment category is the total value of that category as a percentage of net assets available to Common and Preferred Stock.

ABBREVIATIONS:

- PFD. -- Preferred Securities
- PVT. -- Private Placement 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, 2006 THROUGH AUGUST 31, 2007 (UNAUDITED)  
 -----

OPERATIONS:

Net investment income .....  
 Net realized gain/(loss) on investments sold during the period .....  
 Change in net unrealized appreciation/depreciation of investments held during the period .....  
 Distributions to MMP(R)\* Shareholders from net investment income, including changes in accumulated distributions .....  
 NET DECREASE IN NET ASSETS RESULTING FROM OPERATIONS .....

DISTRIBUTIONS:

Dividends paid from net investment income to Common Stock Shareholders(2) .....  
 TOTAL DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS .....

FUND SHARE TRANSACTIONS:

Increase from shares issued under the Dividend Reinvestment and Cash Purchase Plan .....  
 NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK RESULTING FROM FUND SHARE TRANSACTIONS ..

NET DECREASE IN NET ASSETS AVAILABLE TO COMMON STOCK FOR THE PERIOD .....

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 NET ASSETS AVAILABLE TO COMMON STOCK:

Beginning of period .....  
 Net decrease in net assets during the period .....  
 End of period .....

- 
- \* Money Market Cumulative Preferred(TM) Stock.
- (1) These tables summarize the nine months ended August 31, 2007 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2006.
- (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)  
 FOR THE PERIOD FROM DECEMBER 1, 2006 THROUGH AUGUST 31, 2007 (UNAUDITED)  
 FOR A COMMON STOCK SHARE OUTSTANDING THROUGHOUT THE PERIOD.

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PER SHARE OPERATING PERFORMANCE:

Net asset value, beginning of period .....

INVESTMENT OPERATIONS:

Net investment income .....

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

DISTRIBUTIONS TO MMP(R)\* SHAREHOLDERS:

From net investment income .....

From net realized capital gains .....

Total from investment operations .....

DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS:

From net investment income .....

From net realized capital gains .....

Total distributions to Common Stock Shareholders .....

Net asset value, end of period .....

Market value, end of period .....

Common Stock shares outstanding, end of period .....

RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:

Net investment income+ .....

Operating expenses .....

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SUPPLEMENTAL DATA:++

Portfolio turnover rate. ....

Total net assets available to Common and Preferred Stock, end of period (in 000's) .....

Ratio of operating expenses to total average net assets available to Common and Preferred Stock .....

- (1) These tables summarize the nine months ended August 31, 2007 and should be

read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2006.

- \* Money Market Cumulative Preferred(TM) Stock.
- \*\* Annualized.
- \*\*\* Not Annualized.
- + The net investment income ratios reflect income net of operating expenses and payments to MMP(R)\* Shareholders.
- ++ Information presented under heading Supplemental Data includes MMP(R)\*.

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 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, 2006 ..... | \$0.0860                   | \$15.56            | \$16.86               | \$16.02                               |
| January 31, 2007 .....  | 0.0860                     | 15.61              | 17.20                 | 16.34                                 |
| February 28, 2007 ..... | 0.0860                     | 15.80              | 17.25                 | 16.39                                 |
| March 31, 2007 .....    | 0.0860                     | 15.45              | 17.09                 | 16.24                                 |
| April 30, 2007 .....    | 0.0860                     | 15.44              | 16.64                 | 15.81                                 |
| May 31, 2007 .....      | 0.0860                     | 15.18              | 16.00                 | 15.20                                 |
| June 30, 2007 .....     | 0.0860                     | 14.99              | 16.13                 | 15.32                                 |
| July 31, 2007 .....     | 0.0860                     | 14.51              | 15.94                 | 15.14                                 |
| August 31, 2007 .....   | 0.0860                     | 14.19              | 14.13                 | 14.19                                 |

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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.

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 Flaherty & Crumrine Preferred Income Fund Incorporated  
 NOTES TO FINANCIAL STATEMENTS (UNAUDITED)  
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1. AGGREGATE INFORMATION FOR FEDERAL INCOME TAX PURPOSES

At August 31, 2007, the aggregate cost of securities for federal income tax purposes was \$228,556,458, the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was \$9,502,204, and the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was \$9,449,033.

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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

INVESTMENT ADVISER

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

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

- o If your shares are held in a Brokerage Account, contact your Broker.
- o If you have physical possession of your shares in certificate form, contact the Fund's Transfer Agent & Shareholder Servicing Agent --  
PFPC 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, 2007

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