

FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC

Form N-30B-2

April 21, 2006

FLAHERTY & CRUMRINE PREFERRED INCOME FUND

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

The first fiscal quarter of 2006 was a mixed bag for PFD. On the plus side, for the three-month period ended February 28, 2006, the Fund produced a total return on net asset value of +3.8%. Despite this strong investment performance, net income available to shareholders has declined, and the Fund reduced its monthly dividend by 5.0% (from \$0.0905/share to \$0.086/share), beginning with the March distribution. The focus of the Fund is income, so the decision to reduce the dividend was difficult, but necessary.

The total return calculation mentioned above has two basic components--net income earned and net change in principal value. Recently, the latter has done well while the former has come under some pressure.

Net income earned, the amount of investment income left over after payments on the Fund's Money Market Preferred ("MMP(R)") shares and other expenses, is what the Fund can pay out in monthly distributions to common shareholders. Although investment income has increased recently, payments to MMP(R) shares have risen at a faster pace. As a result, the Fund could not continue to distribute common dividends at the same rate.

The MMP(R) rate is closely correlated to other short-term interest rates, all of which have moved up in concert with the Federal Reserve's efforts to influence the pace of economic activity. The MMP(R) rate has risen from a low of 1.02% in April 2004 to 3.35% in March 2006. Despite this jump in rates, the use of MMP(R) leverage continues to add incremental income for common shares because the money we obtain from leverage is being invested in securities with much higher yields.

The other component of total return, principal change, normally is not distributed to common shareholders, but instead is reflected by changes in the Fund's net asset value. During the fiscal period, the Fund's NAV rose 2.0%.

One last comment on total return--whatever the breakdown between net income and principal change, the entire amount belongs to common shareholders. In addition, the two tend to "merge" over time. For example, if principal value increases and the Fund can realize gains, the Fund will have more money to invest and can generate additional income. Or, shareholders can use the income they receive to purchase additional shares via the Dividend Reinvestment Plan to increase the value of their investment.

As readers may recall from previous discussions of market conditions, the preferred securities market has two main segments--issues that pay dividends and those that pay interest. We refer to the first type as "traditional" preferred stock and the second as "hybrid" preferred securities.

Investor demand for traditional preferred stock has been consistently strong for some time now; however new issue supply has not kept up--during the last fiscal quarter there were only two new issues, totaling a meager \$300 million. As a result of this imbalance, this segment has slowly and steadily outperformed other types of fixed-income securities. The solid performance of PFD reflects the portfolio's emphasis on traditional preferred stock.

Although demand for hybrid securities has also been strong for some time, the supply of new hybrid preferred has greatly exceeded the supply of traditional preferred. During the period there were thirty new hybrid issues with a market value of \$13.2 BILLION. As expected, many of these new issues were

## Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

structured like the "ECAP" issues we discussed in our last letter (and on the Fund's website). Even with this sizable amount of new supply, the performance of this segment kept pace with most other types of fixed-income securities during the quarter.

Many of the recent hybrid preferred securities have terms and features that require very close scrutiny. While the basic structure of the enhanced capital security is now fairly well established, with each new issue we are observing small but important differences. This evolutionary process is typical of new structures--our job is to dissect each issue until we fully understand every twist and turn.

The Fund's hedge positions are intended to provide shareholders with some protection against significant increases in long-term interest rates. Over the course of the fiscal quarter, long-term interest rates barely moved, so the hedging strategy had little impact on the Fund's performance. The Fund's hedging strategy did benefit from the "flat" U.S. Treasury yield curve, since the cost of our hedges tends to be lower in this environment.

We hope investors will take advantage of the Fund's website, WWW.PREFERREDINCOME.COM. It contains a wide range of useful and up-to-date information about the Fund. In addition, some of the topics mentioned above are analyzed in greater depth in the Frequently Asked Questions section of the website.

Sincerely,

/s/ Donald F. Crumrine

Donald F. Crumrine  
Chairman of the Board

/s/ Robert M. Ettinger

Robert M. Ettinger  
President

April 17, 2006

-----  
Flaherty & Crumrine Preferred Income Fund Incorporated  
PORTFOLIO OVERVIEW  
FEBRUARY 28, 2006 (UNAUDITED)  
-----

### FUND STATISTICS ON 02/28/06

|                              |    |            |
|------------------------------|----|------------|
| Net Asset Value              | \$ | 15.57      |
| Market Price                 | \$ | 16.65      |
| Premium                      |    | 6.94%      |
| Yield on Market Price        |    | 6.52%      |
| Common Shares<br>Outstanding |    | 10,396,941 |

| MOODY'S RATINGS | % OF PORTFOLIO |
|-----------------|----------------|
| AAA             | 0.7%           |
| AA              | 4.0%           |
| A               | 20.6%          |
| BBB             | 45.9%          |
| BB              | 16.2%          |
| Not Rated       | 11.4%          |

-----

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

Below Investment Grade\* 17.8%

\* 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           | 37%            |
| Banks               | 29%            |
| Financial Services  | 12%            |
| Insurance           | 11%            |
| Oil and Gas         | 4%             |
| REITs               | 4%             |
| Other               | 3%             |

| TOP 10 HOLDINGS BY ISSUER | % OF PORTFOLIO |
|---------------------------|----------------|
| Interstate Power          | 5.3%           |
| Lehman Brothers           | 4.2%           |
| FBOP Corporation          | 3.7%           |
| North Fork Bancorporation | 3.5%           |
| Xcel Energy               | 3.2%           |
| SLM Corporation           | 3.2%           |
| Principal Financial Group | 3.1%           |
| HSBC                      | 2.9%           |
| Cobank                    | 2.8%           |
| Entergy Louisiana         | 2.7%           |

% OF P

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

\*\* 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  
 FEBRUARY 28, 2006 (UNAUDITED)

SHARES/\$ PAR

PREFERRED SECURITIES -- 97.1%  
 BANKING -- 27.8%

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

---

|    |           |   |
|----|-----------|---|
| \$ | 3,000,000 | Astoria Capital Trust I, 9.75% 11/01/29 Capital Security, Series B .....          |
|    | 54,700    | BAC Capital Trust I, 7.00% Pfd. 12/15/31 .....                                    |
| \$ | 750,000   | Barnett Capital II, 7.95% 12/01/26 Capital Security .....                         |
| \$ | 250,000   | Chase Capital I, 7.67% 12/01/26 Capital Security .....                            |
|    | 74,700    | Citigroup Capital VIII, 6.95% Pfd. ....   |
|    |           | Cobank, ACB:  |
|    | 50,000    | 7.00% Pfd., 144A**** .....  |
|    | 75,000    | Adj. Rate Pfd., 144A**** .....  |
| \$ | 500,000   | Comerica (Imperial) Capital Trust I, 9.98% 12/31/26 Capital Security, Series B .. |
|    | 22,300    | BAC Capital Trust III, 7.00% Pfd. ....  |
|    | 9,000     | FBOP Corporation, Adj. Rate Pfd., 144A**** .....                                  |
| \$ | 2,250,000 | First Hawaiian Capital I, 8.343% 07/01/27 Capital Security, Series B .....        |
|    |           | First Republic Bank:  |
|    | 200,000   | 6.25% Pfd. ....   |
|    | 53,700    | 6.70% Pfd. ....   |
| \$ | 1,500,000 | First Union Capital II, 7.95% 11/15/29 Capital Security .....                     |
| \$ | 7,820,000 | GreenPoint Capital Trust I, 9.10% 06/01/27 Capital Security .....                 |
| \$ | 3,000,000 | HBOS Capital Funding LP, 6.85% Pfd. ....  |
|    | 32,625    | HSBC Holdings PLC, 6.20% Pfd., Series A .....                                     |
|    | 5,000     | HSBC Series II, Variable Inverse Pfd., Pvt. ....                                  |
|    | 6,480     | J.P. Morgan Chase & Co., 6.625% Pfd., Series H .....                              |
| \$ | 2,000,000 | Keycorp Capital VII, 5.70% 06/15/35 Capital Security .....                        |
| \$ | 270,000   | Keycorp Institutional Capital B, 8.25% 12/15/26 Capital Security .....            |
| \$ | 674,000   | NB Capital Trust II, 7.83% 12/15/26 Capital Security .....                        |
|    | 16,000    | PFGI Capital Corporation, 7.75% Pfd. ....   |
| \$ | 1,700,000 | RBS Capital Trust B, 6.80% Pfd. ....  |
| \$ | 774,000   | Republic New York Capital II, 7.53% 12/04/26 Capital Security .....               |
|    | 10        | Roslyn Real Estate, 8.95% Pfd., Series C, 144A**** .....                          |
|    | 1,100     | Suntrust Capital V, 7.05% Pfd. 12/15/31 .....                                     |
|    | 87,500    | USB Capital VIII, 6.35% Pfd. 12/29/65 .....                                       |
| \$ | 3,500,000 | Washington Mutual Preferred Funding, Variable Rate Pfd. 03/29/49, 144A**** .....  |
|    | 40,000    | Zions Capital Trust B, 8.00% Pfd. 09/01/32 .....                                  |

---

FINANCIAL SERVICES -- 12.2%

---

|  |         |   |
|--|---------|---|
|  | 141,000 | CIT Group, Inc., 6.35% Pfd., Series A .....           |
|  | 50,000  | Fannie Mae, 4.75% Pfd., Series M .....                |
|  | 53,500  | Goldman Sachs Group, Inc., 6.20% Pfd., Series B ..... |

---

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)

---

SHARES/\$ PAR

---

PREFERRED SECURITIES -- (CONTINUED)  
 FINANCIAL SERVICES -- (CONTINUED)

---

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|         |   |
|---------|---|
|         | Lehman Brothers Holdings, Inc.:                               |
| 43,780  | 5.67% Pfd., Series D .....                                    |
| 154,475 | 5.94% Pfd., Series C .....                                    |
| 3,000   | Merrill Lynch Series II STRIPES Custodial Receipts, Pvt. .... |
| 55,000  | Morgan Stanley Capital Trust VI, 6.60% Pfd. ....              |
| 136,855 | SLM Corporation, 6.97% Pfd., Series A .....                   |

INSURANCE -- 11.3%

|              |   |
|--------------|---|
| 40,000       | ACE Ltd., 7.80% Pfd., Series C .....                                |
|              | Aegon NV:   |
| 40,000       | 6.375% Pfd. ....  |
| 25,000       | 6.50% Pfd. ....   |
| 29,750       | Arch Capital Group Ltd., 8.00%, Pfd. ....                           |
|              | Axis Capital Holdings:  |
| 22,850       | 7.25%, Pfd., Series A .....   |
| 9,300        | Variable Rate Pfd., Series B .....                                  |
| 17,000       | Berkley W.R. Capital Trust II, 6.75% 07/26/45 .....                 |
| 22,000       | Endurance Specialty Holdings, 7.75%, Pfd. ....                      |
| 21,000       | Everest Re Capital Trust II, 6.20% Pfd., Series B .....             |
| 140,000      | MetLife Inc., 6.50% Pfd., Series B .....                            |
| 275,000      | Principal Financial Group, 6.518% Pfd. ....                         |
| \$ 4,000,000 | Provident Financing Trust I, 7.405% 03/15/38 Capital Security ..... |
| 6,300        | Renaissancere Holdings, 7.30% Pfd., Series B .....                  |
| 127,000      | Scottish Re Group Ltd., 7.25% Pfd. ....                             |
| 7,000        | St. Paul Capital Trust I, 7.60% Pfd. ....                           |
| \$ 1,250,000 | USF&G Capital, 8.312% 07/01/46 Capital Security, 144A**** .....     |
| 22,850       | XL Capital Ltd., 8.00% Pfd. Series A .....                          |

UTILITIES -- 35.6%

|         |   |
|---------|---|
|         | Alabama Power Company:  |
| 300     | 4.52% Pfd. ....   |
| 5,734   | 4.72% Pfd. ....   |
| 200,000 | 5.30% Pfd. ....   |
| 10,000  | Baltimore Gas & Electric Company, 6.70% Pfd., Series 1993 ..... |
|         | Central Hudson Gas & Electric Corporation:                      |
| 5,000   | 4.35% Pfd., Series D, Pvt. ....                                 |
| 900     | 4.96% Pfd., Series E, Pvt. ....                                 |

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)

SHARES/\$ PAR

PREFERRED SECURITIES -- (CONTINUED)

UTILITIES -- (CONTINUED)

---

|              |   |
|--------------|---|
| 11,119       | Central Vermont Public Service Corporation, 8.30% Sinking Fund Pfd., Pvt. ....  |
|              | Connecticut Light & Power Company:  |
| 2,124        | 4.50% Pfd., Pvt. ....   |
| 34,300       | 5.28% Pfd., Series 1967 .....   |
| 1,905        | 6.56% Pfd., Series 1968 .....   |
| 15,778       | \$3.24 Pfd. ....  |
| 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 .....                      |
| \$ 1,500,000 | Dominion Resources Capital Trust III, 8.40% 01/15/31 .....                      |
|              | Duquesne Light Company:   |
| 7,675        | 4.10% Pfd. ....   |
| 9,190        | 4.15% Pfd. ....   |
| 910          | 4.20% Pfd. ....   |
| 40,575       | 6.50% Pfd. ....   |
| 5,490        | \$2.10 Pfd., Series A .....   |
| 5,000        | Energy East Capital Trust I, 8.25% Pfd. ....                                    |
|              | Entergy Arkansas, Inc.:   |
| 5,574        | 7.32% Pfd. ....   |
| 11,350       | 7.40% Pfd. ....   |
| 6,253        | 7.80% Pfd. ....   |
| 3,822        | 7.88% Pfd. ....   |
| 30,266       | \$1.96 Pfd. ....  |
| 4,555        | Entergy Gulf States, Inc., 7.56% Pfd. ....                                      |
|              | Entergy Louisiana, Inc.:  |
| 36,000       | 6.95% Pfd., 144A**** .....  |
| 260          | 7.84% Pfd. ....   |
| 106,538      | 8.00% Pfd., Series 92 .....   |
| 5,000        | Entergy Mississippi, Inc., 4.92% Pfd. ....                                      |
|              | Florida Power Company:  |
| 5,157        | 4.60% Pfd. ....   |
| 18,535       | 4.75% Pfd. ....   |
| 50,000       | Georgia Power Capital Trust V, 7.125% Pfd. ....                                 |
| 2,010        | Great Plains Energy, Inc., 4.50% Pfd. ....                                      |
| 24,000       | Gulf Power Company, 6.00% Pfd., Series 1 .....                                  |
| \$ 3,500,000 | Houston Light & Power Capital Trust II, 8.257%, 02/01/37 Capital Security ..... |
| 32,650       | Indianapolis Power & Light Company, 5.65% Pfd. ....                             |
| 384,000      | Interstate Power & Light Company, 8.375% Pfd., Series B .....                   |
| 14,250       | Narragansett Electric Company, 4.64% Pfd. ....                                  |

---

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)

---

SHARES/\$ PAR

PREFERRED SECURITIES -- (CONTINUED)  
 UTILITIES -- (CONTINUED)

---

Northern Indiana Public Service Company:

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|    |         |   |  |
|----|---------|---|--|
|    | 3,905   | 7.44% Pfd. ....   |  |
|    | 7,465   | Adj. Rate Pfd., Series A .....                                      |  |
|    | 6,170   | Ohio Edison Company, 4.44% Pfd. ....                                |  |
|    |         | 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. ....  |  |
|    | 12,333  | \$7.48 Sinking Fund Pfd. ....                                       |  |
|    | 9,666   | Portland General Electric, 7.75% Sinking Fund Pfd. ....             |  |
|    | 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. ....  |  |
|    | 13,100  | Savannah Electric & Power Company, 6.00% Pfd. ....                  |  |
|    |         | South Carolina Electric & Gas Company:                              |  |
|    | 25,373  | 5.125% Purchase Fund Pfd., Pvt. ....                                |  |
|    | 6,703   | 6.00% Purchase Fund Pfd., Pvt. ....                                 |  |
|    | 54,100  | Southern California Edison, 4.08% Pfd. ....                         |  |
|    | 75,000  | Southern Union Company, 7.55% Pfd. ....                             |  |
| \$ | 750,000 | TXU Electric Capital V, 8.175% 01/30/37 Capital Security .....      |  |
|    |         | Union Electric Company:   |  |
|    | 14,150  | 4.56% Pfd. ....   |  |
|    | 4,000   | \$7.64 Pfd. ....  |  |
|    | 12,500  | Virginia Electric & Power Company, \$7.05 Pfd. ....                 |  |
|    | 11,200  | Virginia Power Capital Trust, 7.375% Pfd. 07/30/42 .....            |  |
|    |         | Wisconsin Power & Light Company:                                    |  |
|    | 1,220   | 4.50% Pfd. ....   |  |
|    | 546     | 4.80% Pfd. ....   |  |
|    | 13,000  | 6.20% Pfd. ....   |  |

-----  
 Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)  
 -----

SHARES/\$ PAR  
 -----

PREFERRED SECURITIES -- (CONTINUED)  
 UTILITIES -- (CONTINUED)  
 -----

|  |        |                             |  |
|--|--------|-----------------------------|--|
|  |        | Xcel Energy, Inc.:          |  |
|  | 16,030 | \$4.08 Pfd., Series B ..... |  |
|  | 26,200 | \$4.10 Pfd., Series C ..... |  |

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|        |                             |
|--------|-----------------------------|
| 22,000 | \$4.11 Pfd., Series D ..... |
| 17,750 | \$4.16 Pfd., Series E ..... |
| 10,000 | \$4.56 Pfd., Series G ..... |

OIL AND GAS -- 4.2%

|              |   |
|--------------|---|
| 8,000        | Devon Energy Corporation, 6.49% Pfd., Series A .....        |
| 5,985        | EOG Resources, Inc., 7.195% Pfd., Series B .....            |
| \$ 1,675,000 | KN Capital Trust III, 7.63% 04/15/28 Capital Security ..... |
| 10,000       | Lasmo America Limited, 8.15% Pfd., 144A**** .....           |

REAL ESTATE INVESTMENT TRUST (REIT) -- 4.1%

|         |   |
|---------|---|
| 31,000  | AMB Property Corporation, 7.00%, Pfd., REIT, Series O .....     |
|         | Duke Realty Corporation:  |
| 15,000  | 6.50% Pfd., REIT, Series K .....                                |
| 20,000  | 6.625% Pfd., REIT, Series J .....                               |
| 1,000   | Equity Residential Properties, 8.29% Pfd., REIT, Series K ..... |
| 50,000  | HRPT Properties Trust, 7.125% Pfd., REIT, Series C .....        |
|         | PS Business Parks, Inc.:  |
| 16,000  | 7.00% Pfd., REIT, Series H .....                                |
| 20,000  | 7.20% Pfd., REIT, Series M .....                                |
|         | Public Storage, Inc.:   |
| 13,300  | 6.18% Pfd., REIT, Series D .....                                |
| 109,270 | 6.45% Pfd., REIT, Series F .....                                |
| 10,000  | 6.45% Pfd., REIT, Series X .....                                |
| 22,500  | 6.75% Pfd., REIT, Series E .....                                |
| 3,500   | 7.125% Pfd., REIT .....   |
| 40,000  | Realty Income Corporation, 7.375% Pfd., REIT, Series D .....    |
|         | Regency Centers Corporation:                                    |
| 7,600   | 6.70% Pfd., REIT .....  |
| 40,000  | 7.25% Pfd., REIT .....  |

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)

SHARES/\$ PAR

PREFERRED SECURITIES -- (CONTINUED)  
 MISCELLANEOUS INDUSTRIES -- 1.9%

|        |  |
|--------|--|
| 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**** .....        |



Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|                                   |   |
|-----------------------------------|---|
| 26,000                            | Touch America Holdings, \$6.875 Pfd. ....     |
| -----                             |   |
|                                   | TOTAL PREFERRED SECURITIES                    |
|                                   | (Cost \$218,142,479) .....                    |
| CORPORATE DEBT SECURITIES -- 1.1% |   |
|                                   | OIL AND GAS -- 0.2%                           |
| -----                             |   |
| 15,000                            | Nexen, Inc., 7.35% Subordinated Notes .....   |
| -----                             |   |
|                                   | UTILITIES -- 0.9%                             |
| -----                             |   |
| \$1,000,000                       | Duquesne Light Holdings, 6.25% 08/15/35 ..... |
| 45,000                            | Northern States Power Company, 8.00% .....    |
| -----                             |   |
|                                   | TOTAL CORPORATE DEBT SECURITIES               |
|                                   | (Cost \$2,492,012) .....                      |
| COMMON STOCK -- 0.8%              |   |
|                                   | BANKING -- 0.8%                               |
| -----                             |   |
| 110,000                           | New York Community Bancorp, Inc. ....         |
| -----                             |   |
|                                   | TOTAL COMMON STOCK                            |
|                                   | (Cost \$1,917,807) .....                      |

-----

Flaherty & Crumrine Preferred Income Fund Incorporated  
 PORTFOLIO OF INVESTMENTS (CONTINUED)  
 FEBRUARY 28, 2006 (UNAUDITED)

-----

SHARES/\$ PAR

-----

|                           |   |
|---------------------------|---|
| OPTION CONTRACTS -- 0.4%  |   |
| 250                       | April Put Options on June U.S. Treasury Bond Futures, Expiring 03/24/06 ..... |
| 391                       | June Put Options on June U.S. Treasury Bond Futures, Expiring 05/26/06 .....  |
| 884                       | June Put Options on June U.S. Treasury Bond Futures, Expiring 05/26/06 .....  |
| -----                     |   |
|                           | TOTAL OPTION CONTRACTS  |
|                           | (Cost \$1,170,466) .....  |
| MONEY MARKET FUND -- 1.3% |   |
| 3,266,070                 | BlackRock Provident Institutional, TempFund .....                             |

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

---

|   |        |
|---|--------|
| TOTAL MONEY MARKET FUND<br>(Cost \$3,266,070) .....                         |        |
| TOTAL INVESTMENTS (Cost \$226,988,834***) .....                             | 100.7% |
| OTHER ASSETS AND LIABILITIES (Net) .....                                    | (0.7)  |
| TOTAL NET ASSETS AVAILABLE TO COMMON AND PREFERRED STOCK .....              | 100.0% |
| 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.

\*\*\* 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.

+ 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:

REIT -- Real Estate Investment Trust

PFD. -- Preferred Securities

PVT. -- Private Placement Securities

---

Flaherty & Crumrine Preferred Income Fund Incorporated  
STATEMENT OF CHANGES IN NET ASSETS AVAILABLE TO COMMON STOCK(1)  
FOR THE PERIOD FROM DECEMBER 1, 2005 THROUGH FEBRUARY 28, 2006 (UNAUDITED)

---

OPERATIONS:

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|   |         |
|---|---------|
| Net investment income .....   | \$ 3,   |
| Net realized gain/(loss) on investments sold during the period .....  |         |
| Change in net unrealized appreciation/depreciation of investments held<br>during the period .....   | 3,      |
| Distributions to Money Market Cumulative Preferred(TM) Stock<br>Shareholders from net investment income, including changes in<br>accumulated undeclared distributions ..... | (       |
| -----   |         |
| NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS .....  | 6,      |
| DISTRIBUTIONS:  |         |
| Dividends paid from net investment income to Common Stock Shareholders (2) .....  | (2,     |
| -----   |         |
| TOTAL DISTRIBUTIONS TO COMMON STOCK SHAREHOLDERS .....  | (2,     |
| FUND SHARE TRANSACTIONS:  |         |
| Increase from shares issued under the Dividend Reinvestment<br>and Cash Purchase Plan .....   |         |
| -----   |         |
| NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK RESULTING<br>FROM FUND SHARE TRANSACTIONS .....  |         |
| -----   |         |
| NET INCREASE IN NET ASSETS AVAILABLE TO COMMON STOCK<br>FOR THE PERIOD .....  | \$ 3,   |
| =====   |         |
| -----   |         |
| NET ASSETS AVAILABLE TO COMMON STOCK:   |         |
| Beginning of period .....   | \$ 158, |
| Net increase in net assets during the period .....  | 3,      |
| -----   |         |
| End of period .....   | \$ 161, |
| =====   |         |

- 
- (1) These tables summarize the three months ended February 28, 2006 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2005.
  - (2) May include income earned, but not paid out, in prior fiscal year.

-----

Flaherty & Crumrine Preferred Income Fund Incorporated  
 FINANCIAL HIGHLIGHTS(1)  
 FOR THE PERIOD FROM DECEMBER 1, 2005 THROUGH FEBRUARY 28, 2006 (UNAUDITED)  
 FOR A COMMON SHARE OUTSTANDING THROUGHOUT THE PERIOD.  
 -----

PER SHARE OPERATING PERFORMANCE:  
 Net asset value, beginning of period .....

INVESTMENT OPERATIONS:  
 Net investment income .....

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

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 shares outstanding, end of period .....

RATIOS TO AVERAGE NET ASSETS AVAILABLE TO COMMON STOCK SHAREHOLDERS:

Net investment income+ .....

Operating expenses .....

-----

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 three months ended February 28, 2006 and should be read in conjunction with the Fund's audited financial statements, including footnotes, in its Annual Report dated November 30, 2005.

\* 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)\*.

-----

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, 2005 ..... | \$0.0905                   | \$15.38            | \$16.09               | \$15.38                               |

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

|                         |        |       |       |       |
|-------------------------|--------|-------|-------|-------|
| January 31, 2006 .....  | 0.0905 | 15.43 | 16.89 | 16.05 |
| February 28, 2006 ..... | 0.0905 | 15.57 | 16.65 | 15.82 |

-----  
(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 payment 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.

13

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

1. AGGREGATE INFORMATION FOR FEDERAL INCOME TAX PURPOSES

At February 28, 2006, the aggregate cost of securities for federal income tax purposes was \$227,273,792, the aggregate gross unrealized appreciation for all securities in which there is an excess of value over tax cost was \$19,742,322 and the aggregate gross unrealized depreciation for all securities in which there is an excess of tax cost over value was \$3,478,062.

14

[This page intentionally left blank]

[LOGO] Flaherty & Crumrine  
=====

PREFERRED INCOME FUND

Quarterly  
Report

February 28, 2006

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

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

Edgar Filing: FLAHERTY & CRUMRINE PREFERRED INCOME FUND INC - Form N-30B-2

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  
Christopher D. Ryan, CFA  
Vice President  
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.