PROGRESSIVE RETURN FUND INC
Form 497
September 24, 2002

PROGRESSIVE RETURN FUND, INC.
c/o Bear Stearns Funds Management Inc.
383 Madison Avenue
New York, New York 10179
September 13, 2002

Dear Stockholder:

We are pleased to invite you to the special meeting of stockholders (the "PGF Special Meeting") of Progressive Return Fund, Inc., a Maryland corporation. Progressive Return Fund, Inc. is sometimes referred to herein as "PGF" or the "Fund."

The PGF Special Meeting is scheduled to be held at 11:00 a.m., Eastern time, on Friday, October 11, 2002, at the offices of Bear Stearns Funds Management Inc., 383 Madison Avenue, New York, New York 10179.

The Board of Directors has called this Meeting to vote on a Merger Agreement and Plan of Reorganization (the "Plan" or "Merger Agreement"), whereby Cornerstone Strategic Value Fund, Inc. ("CLM") will merge with and into PGF in accordance with the Maryland General Corporation Law (the "Merger"), and on an amendment to the Fund's Articles of Incorporation changing the name of the Fund from "Progressive Return Fund, Inc." to "Progressive Total Return Fund, Inc."

The Board of Directors of PGF believes that the Merger and name change are very important to your interests as a stockholder.

The combined Fund will approximately double the size of PGF and the Board of Directors believes that this will enable:

(1) a lower operating expense ratio, and
(2) enhanced market liquidity.

Stockholders who are unable to attend this meeting are strongly encouraged to vote by proxy, which is customary in corporate meetings of this kind. A Proxy Statement/Prospectus regarding the meeting, a proxy card(s) for your vote at the meeting and an envelope - postage prepaid - in which to return your proxy card are enclosed. At the PGF Special Meeting you will be asked to vote on two matters.

The proposed merger of the Funds is described in more detail in the combined Proxy Statement/Prospectus.

THE BOARD OF DIRECTORS OF PGF BELIEVES THAT THE PROPOSED MERGER AND THE NAME CHANGE ARE IN THE BEST INTERESTS OF THE STOCKHOLDERS AND RECOMMENDS THAT YOU READ THE ENCLOSED MATERIALS CAREFULLY AND THEN VOTE "FOR" PROPOSALS 1 AND 2.

Your vote is important. To approve the Merger the affirmative vote of a majority of PGF's outstanding shares is required. Therefore, a failure to vote would amount to a vote against the Merger. PLEASE TAKE A MOMENT NOW TO SIGN AND RETURN

YOUR PROXY CARD(S) IN THE ENCLOSED POSTAGE-PAID RETURN ENVELOPE

Respectfully,

Ralph W. Bradshaw
Chairman of the Board of Directors

YOU ARE URGED TO SIGN THE PROXY CARD(S) AND RETURN THE CARD(S) IN THE POSTAGE-PAID ENVELOPE TO ENSURE A QUORUM AT THE MEETING. YOUR VOTE IS IMPORTANT REGARDLESS OF THE SIZE OF YOUR SHAREHOLDINGS.

CORNERSTONE STRATEGIC VALUE FUND, INC.
c/o Bear Stearns Funds Management, Inc.
383 Madison Avenue
New York, New York 10179
September 13, 2002

Dear Stockholder:

We are pleased to invite you to the Annual Meeting of Stockholders (the "CLM Annual Meeting") of Cornerstone Strategic Value Fund, Inc., a Maryland corporation. Cornerstone Strategic Value Fund, Inc. is sometimes referred to hereinafter as "CLM" or the "Fund."

The CLM Annual Meeting is scheduled to be held at 11:30 a.m., Eastern time, on Friday, October 11, 2002, at the offices of Bear Stearns Funds Management Inc., 383 Madison Avenue, New York, New York 10179.

First, you will be asked to vote on a Merger Agreement and Plan of Reorganization (the "Merger Agreement"), whereby CLM will merge with and into Progressive Return Fund, Inc. ("PGF") in accordance with the Maryland General Corporation Law (the "Merger"). As a result of the Merger:

o CLM will no longer exist,
o PGF will be the surviving corporation,
o each share of common stock of CLM will convert into an equivalent dollar amount of full shares and fractional shares of common stock of PGF to all CLM stockholders that participate in CLM's dividend reinvestment plan, based on the net asset value per share of each fund on the date the Merger is consummated, and
o CLM stockholders that do not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares.

The combined Fund will approximately double the size of CLM and the Board of Directors believes that this will enable:

(1) a lower operating expense ratio, and
(2) enhanced market liquidity.

The proposed merger and the investment policies of the Funds are described in more detail in the combined Proxy Statement/Prospectus.

CLM's Stockholders are also being asked to vote contingently on three additional proposals. Votes on these proposals will be implemented only in the event that the Merger is not consummated.

The second Proposal that CLM Stockholders will be asked to vote on, and which will take effect only if the Merger proposal is not consummated, will be the election of two (2) Class I nominees standing for re-election to CLM's Board of Directors, Messrs. Ralph W. Bradshaw and Edwin Meese III.

The third Proposal that CLM Stockholders will be asked to vote on, and which will take effect only if the Merger proposal is not consummated, is the ratification of the selection of Tait, Weller & Baker as the Fund's independent accountants for the year ending December 31, 2002.

The fourth Proposal being submitted to CLM Stockholders, and which, if passed, will be further addressed by the Fund's Board of Directors only if the Merger proposal is not consummated, is a stockholder proposal requesting that within 90 days after the CLM Annual Meeting, CLM be converted into an open-end fund.

Stockholders who are unable to attend this meeting are strongly encouraged to vote by proxy, which is customary in corporate meetings of this kind. A Proxy Statement/Prospectus regarding the meeting, a proxy card(s) for your vote at the meeting and an envelope - postage prepaid - in which to return your proxy card are enclosed. At the CLM Annual Meeting you will be asked to vote on four matters.

THE BOARD OF DIRECTORS OF CLM BELIEVES THAT THE PROPOSED MERGER IS IN THE BEST INTERESTS OF CLM AND ITS STOCKHOLDERS AND RECOMMENDS THAT YOU READ THE ENCLOSED MATERIALS CAREFULLY AND THEN VOTE "FOR" PROPOSAL 1.

THE BOARD OF DIRECTORS OF CLM BELIEVES THAT, IN THE ALTERNATIVE, IF THE PROPOSED MERGER IS NOT CONSUMMATED, CONTINGENT PROPOSALS 2 AND 3, THE RE-ELECTION OF THE TWO CLASS I DIRECTORS AND THE RATIFICATION OF THE SELECTION OF TAIT, WELLER & BAKER, ARE IN THE BEST INTERESTS OF CLM AND ITS STOCKHOLDERS AND RECOMMENDS THAT YOU READ THE ENCLOSED MATERIALS CAREFULLY AND THEN VOTE "FOR" PROPOSALS 2 AND 3.

THE BOARD OF DIRECTORS OF CLM BELIEVES THAT THE STOCKHOLDER PROPOSAL IS NOT IN THE BEST INTERESTS OF THE STOCKHOLDERS AND RECOMMENDS THAT YOU VOTE "AGAINST" PROPOSAL 4.

Your vote is important. To approve the Merger the affirmative vote of a majority of CLM's outstanding shares is required. Therefore, a failure to vote would amount to a vote against the Merger. PLEASE TAKE A MOMENT NOW TO SIGN AND RETURN YOUR PROXY CARD(S) IN THE ENCLOSED POSTAGE-PAID RETURN ENVELOPE

Respectfully,

Ralph W. Bradshaw,
Chairman of the Board of Directors

YOU ARE URGED TO SIGN THE PROXY CARD(S) AND RETURN THE CARD(S) IN THE

POSTAGE-PAID ENVELOPE TO ENSURE A QUORUM AT THE MEETING. YOUR VOTE IS IMPORTANT REGARDLESS OF THE SIZE OF YOUR SHAREHOLDINGS.

PROGRESSIVE RETURN FUND, INC.
NOTICE OF SPECIAL MEETING OF STOCKHOLDERS

Notice is hereby given that the Special Meeting of Stockholders (the "PGF Special Meeting") of Progressive Return Fund, Inc. ("PGF"), a Maryland corporation, will be held at the offices of Bear Stearns Funds Management Inc., 383 Madison Avenue, New York, New York 10179, on Friday, October 11, 2002, at 11:00 a.m., Eastern time, for the following purposes:

1. To consider and vote upon the approval of a Merger Agreement and Plan of Reorganization dated October 11, 2002 whereby Cornerstone Strategic Value Fund, Inc. ("CLM"), a Maryland corporation, will merge with and into PGF in accordance with the Maryland General Corporation Law;

and the stockholders of PGF will be asked to vote upon PGF Proposal 2, which is conditional on the consummation of the Merger:

2. To amend the Articles of Incorporation to change the name of the Fund from "Progressive Return Fund, Inc." to "Progressive Total Return Fund, Inc."

The appointed proxies will vote in their discretion on any other business that may properly come before the PGF Special Meeting or any adjournments thereof.

Holders of record of shares of common stock of PGF at the close of business on September 6, 2002 (the "Record Date") are entitled to vote at the PGF Special Meeting and at any postponements or adjournments thereof. CLM stockholders must approve the merger as well.

The persons named as proxies may propose one or more adjournments of the PGF Special Meeting if the necessary quorum to transact business or the vote required to approve or reject any proposal is not obtained at the meeting. Any such adjournment will require the affirmative vote of the holders of a majority of PGF's shares present in person or by proxy at the PGF Special Meeting. The persons named as proxies will vote those proxies which they are entitled to vote on any such proposal in accordance with their best judgment in the interest of PGF.

The presence, either in person or by proxy, of the holders of one-third of the outstanding shares of common stock entitled to vote at a meeting of either Fund, will constitute a quorum for the transaction of business by that Fund. For purposes of determining the presence of a quorum for transacting business at a meeting, abstentions and broker "non-votes" will be treated as shares that are present but will not be voted as to any matters being considered at the Meeting. Broker non-votes are proxies received by a Fund from brokers or nominees, indicating that the broker or nominee has neither received instructions from the beneficial owner or other persons entitled to vote nor has the discretionary power to vote on a particular matter. Stockholders are urged to forward their voting instructions promptly.

The enclosed proxy is being solicited on behalf of the Board of Directors of PGF.

By Order of the Board of Directors,

Ralph W. Bradshaw, President

Important -- We urge you to sign and date the enclosed proxy card(s) and return the card(s) in the enclosed addressed envelope which requires no postage and is intended for your convenience. Your prompt return of the enclosed proxy card(s) may save the necessity and expense of further solicitations to ensure a quorum at the PGF Special Meeting. If you can attend the PGF Special Meeting and wish to vote your shares in person at that time, you will be able to do so.

CORNERSTONE STRATEGIC VALUE FUND, INC.
NOTICE OF ANNUAL MEETING OF STOCKHOLDERS

Notice is hereby given that the Annual Meeting of Stockholders (the "CLM Annual Meeting") of Cornerstone Strategic Value Fund, Inc. ("CLM"), a Maryland corporation, will be held at the offices of Bear Stearns Funds Management Inc., 383 Madison Avenue, New York, New York 10179, on Friday, October 11, 2002, at 11:30 a.m., Eastern time, for the following purposes:

1. To consider and vote upon the approval of a Merger Agreement and Plan of Reorganization dated October 11, 2002 whereby CLM will merge with and into Progressive Return Fund, Inc. ("PGF"), a Maryland corporation, in accordance with the Maryland General Corporation Law;

and, in the alternative if the Merger proposal is not consummated, Stockholders are asked to vote upon Proposals 2, 3 and 4:

2. To consider and vote upon the election of two (2) Class I nominees standing for re-election to CLM's Board of Directors, Messrs. Ralph W. Bradshaw and Edwin Meese III;

3. To ratify the selection of Tait, Weller & Baker as the Fund's independent accountants for the year ending December 31, 2002; and

4. To consider and vote upon a stockholder proposal requesting that CLM be converted into an open-end fund.

The appointed proxies will vote in their discretion on any other business that may properly come before the CLM Annual Meeting or any adjournments thereof.

Holders of record of shares of common stock of CLM at the close of business on September 6, 2002 (the "Record Date") are entitled to vote at the CLM Annual Meeting and at any postponements or adjournments thereof. PGF stockholders must approve the merger as well.

The persons named as proxies may propose one or more adjournments of

the CLM Annual Meeting if the necessary quorum to transact business or the vote required to approve or reject any proposal is not obtained at the meeting. Any such adjournment will require the affirmative vote of the holders of a majority of CLM's shares present in person or by proxy at the CLM Annual Meeting. The persons named as proxies will vote those proxies which they are entitled to vote on any such proposal in accordance with their best judgment in the interest of CLM.

The presence, either in person or by proxy, of the holders of one-third of the outstanding shares of common stock entitled to vote at a meeting of either Fund, will constitute a quorum for the transaction of business by that Fund. For purposes of determining the presence of a quorum for transacting business at a meeting, abstentions and broker "non-votes" will be treated as shares that are present but will not be voted as to any matters being considered at the Meeting. Broker non-votes are proxies received by a Fund from brokers or nominees, indicating that the broker or nominee has neither received instructions from the beneficial owner or other persons entitled to vote nor has the discretionary power to vote on a particular matter. Stockholders are urged to forward their voting instructions promptly.

The enclosed proxy is being solicited on behalf of the Board of Directors of CLM.

By Order of the Board of Directors,

Ralph W. Bradshaw, President

Important -- We urge you to sign and date the enclosed proxy card(s) and return the card(s) in the enclosed addressed envelope which requires no postage and is intended for your convenience. Your prompt return of the enclosed proxy card(s) may save the necessity and expense of further solicitations to ensure a quorum at the CLM Annual Meeting. If you can attend the CLM Annual Meeting and wish to vote your shares in person at that time, you will be able to do so.

INSTRUCTIONS FOR SIGNING PROXY CARDS

The following general rules for signing proxy cards may be of assistance to you and avoid the time and expense to the Fund involved in validating your vote if you fail to sign your proxy card properly.

1. Individual Accounts: Sign your name exactly as it appears in the registration on the proxy card.

2. Joint Accounts: Either party may sign, but the name of the party signing should conform exactly to a name shown in the registration.

3. Other Accounts: The capacity of the individual signing the proxy card should be indicated unless it is reflected in the form of registration. For example:

REGISTRATION

CORPORATE ACCOUNTS	VALID SIGNATURE
(1) ABC Corp................................	ABC Corp. (by John Doe, Treasurer)
(2) ABC Corp................................	John Doe, Treasurer
(3) ABC Corp. c/o John Doe, Treasurer.................	John Doe
(4) ABC Corp. Profit Sharing Plan...........	John Doe, Trustee
TRUST ACCOUNTS	
(1) ABC Trust...............................	Jane B. Doe, Trustee
(2) Jane B. Doe, Trustee u/t/d/ 12/28/78.........................	Jane B. Doe
CUSTODIAL OR ESTATE ACCOUNTS	
(1) John B. Smith, Cust. f/b/o John B. Smith, Jr. UGMA...........	John B. Smith
(2) John B. Smith...........................	John B. Smith, Jr., Executor

CORNERSTONE STRATEGIC VALUE FUND, INC.
383 Madison Avenue
New York, New York 10179
Tel: (212) 272-2093

TO BE MERGED WITH AND INTO

PROGRESSIVE RETURN FUND, INC.
383 Madison Avenue
New York, New York 10179
Tel: (212) 272-2093

COMBINED PROXY STATEMENT/PROSPECTUS

This combined Proxy Statement/Prospectus is being furnished to stockholders of Progressive Return Fund, Inc. ("PGF") and Cornerstone Strategic Value Fund, Inc. ("CLM") for use at PGF's Special Meeting and CLM's Annual Meeting each to be held on Friday, October 11, 2002 at 11:00 a.m. and 11:30 a.m. Eastern time, respectively, and at any and all postponements or adjournments thereof. Hereinafter the PGF Special Meeting of Stockholders and the CLM Annual Meeting of Stockholders shall be collectively referred to as the "Meetings." The approximate mailing date of this Proxy Statement/Prospectus is September 13, 2002.

PURPOSE OF THE MEETINGS.

At each of the Meetings, stockholders will be asked to approve a Merger Agreement and Plan of Reorganization dated October 11, 2002 (the "Plan") whereby CLM will merge with and into PGF, in accordance with the Maryland General Corporation Law (the "Merger"). In addition, PGF stockholders will be asked to approve the amendment to PGF's Articles of Incorporation changing the

name of the Fund in the event that the Merger is consummated. In the event that the Merger is not consummated, CLM's stockholders will be asked to contingently vote on the re-election of two nominees to CLM's Board of Directors, the ratification of Tait, Weller & Baker as the Fund's independent accountants for the year ending December 31, 2002, and a stockholder's proposal requesting that the Fund be open-ended.

SPECIFICS OF THE PLAN.

As a result of the merger:

- CLM will no longer exist,
- PGF will be the surviving corporation, and
- each share of common stock of CLM will convert into an equivalent dollar amount of full shares and fractional shares of common stock of PGF to all CLM stockholders that participate in CLM's dividend reinvestment plan, based on

-1-

the net asset value per share of each fund on the date the Merger is consummated, and - CLM stockholders that do not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares.

In connection with the merger, PGF will issue that number of shares that have an aggregate net asset value equal to the aggregate net asset value of the outstanding shares of CLM. Each CLM stockholder, in connection with the Merger, will receive shares of PGF having an aggregate net asset value equal to the aggregate net asset value of the stockholder's CLM shares at the close of business on the day before the Effective Date of the Merger. While the total net asset value of shares received by each CLM stockholder in the Merger may be the same as before the Merger, the market value of PGF shares that a CLM stockholder receives in the Merger will be more or less than the market value of CLM shares that such stockholder owns immediately before the Merger, depending on the current market discount levels of CLM and PGF.

If the Merger proposal is approved, CLM stockholders will become stockholders of a non-diversified rather than a diversified management investment company. PGF, as a non-diversified investment management company, may invest a larger proportion of its assets in a single issuer while CLM, as a diversified management investment company, can not. Thus, an investment in PGF, as a non-diversified investment company, may present a greater risk to an investor than an investment in CLM, as a diversified company, because of the possibility of a greater investment of assets in one issuer.

PGF and CLM are both registered with the Securities Exchange Commission as closed-end management investment companies and are both listed on the New York Stock Exchange ("NYSE"). PGF seeks total return consisting of capital appreciation and current income by investing primarily in U.S. and non-U.S. equity and debt securities. CLM's investment objective is to seek long-term capital appreciation through investment in equity securities of U.S. and non-U.S. companies. The current investment objective and policies of PGF will continue unchanged if the merger occurs.

The terms and conditions of the merger and related transactions are more fully described in this Proxy Statement/Prospectus and in the Plan, a copy of which is attached hereto as Exhibit A.

This Proxy Statement/Prospectus serves as a prospectus for shares of PGF under the Securities Act of 1933, as amended (the "Securities Act"), in connection with the issuance of PGF common shares in the merger.

Assuming the stockholders of each Fund approve the merger and that all other conditions contained in the Merger Agreement are satisfied or waived,

the Funds will jointly file articles of merger (the "Articles of Merger"), with the State Department of Assessments and Taxation of Maryland (the "Department"). The merger will become effective on October 14, 2002, or such other date as may result from the application of the terms of the Merger Agreement (the "Effective Date"). CLM, as soon as practicable after the Effective Date, will terminate its registration under the Investment Company Act of 1940, as amended (the "Investment Company Act").

Under Section 3-202 of the Maryland General Corporation law, shareholders of PGF and CLM are not entitled to any appraisal or similar rights in connection with the merger contemplated by the Plan.

You should retain this Proxy Statement/Prospectus for future reference as it sets forth concisely information about PGF and CLM that you should know before voting on the proposals described below.

A Statement of Additional Information (the "SAI") dated September 13, 2002, which contains additional information about the merger and the Funds has been filed with the Securities and Exchange Commission (the "SEC"). The SAI and financial statements of PGF and CLM for the fiscal year ended December 31, 2001 and for the period ended June 30, 2002 are incorporated by reference into this Proxy Statement/Prospectus. Please note that each Fund's semi-annual reports for the period ending June 30, 2002 are available. Copies of these documents are available upon request and without charge by writing to the Secretary of the Fund c/o Bear Stearns Funds Management Inc. located at 383 Madison Avenue, 23rd Floor, New York, New York 10179, or by calling (212) 272-2093 or 1-866-227-3400.

PGF's shares of common stock are listed on the NYSE under the symbol "PGF" and CLM's shares of common stock are listed on the NYSE under the symbol "CLM". After the Effective Date, shares of common stock of PGF will continue to be listed on the NYSE under the symbol "PGF". Reports, proxy materials and other information concerning each Fund may be inspected at the offices of the NYSE, 20 Broad Street, New York, New York 10005.

The SEC has not approved or disapproved these securities or determined if this Proxy Statement/Prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

The date of this Proxy Statement/Prospectus is September 13, 2002

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Exhibit B: Certificate of Amendment to the Articles of Incorporation B-1

GENERAL

This combined Proxy Statement/Prospectus is furnished to the stockholders of each Fund in connection with the solicitation of proxies on behalf of each of the Boards of Directors of the Funds. The Board of Directors of each Fund is soliciting proxies for use at each Fund's respective Meeting. The mailing address for both Funds is c/o Bear Stearns Funds Management Inc., 383 Madison Avenue, New York, New York 10179.

This Proxy Statement/Prospectus, the Notices of Meeting to Stockholders and the proxy card(s) (attached hereto as Exhibit B) are first being mailed to stockholders on or about September 13, 2002 or as soon as practicable thereafter. Any stockholder who gives a proxy has the power to revoke the proxy either: (i) by mail, addressed to the Secretary of the respective Fund, at the Fund's mailing address, or (ii) in person at the Meeting by executing a superseding proxy or by submitting a notice of revocation to the respective Fund. All properly executed proxies received in time for the meetings will be voted as specified in the proxy or, if no specification is made, "FOR" each proposal for that Fund, except that in the case of Proposal 4, all unspecified proxies will be voted "AGAINST" such Stockholder Proposal.

Stockholders of both PGF and CLM are being asked to vote on Proposal 1 -- the approval of the Plan. Contingent on consummation of the Merger, PGF stockholders are being asked to authorize an amendment to PGF's Articles of Incorporation changing the name of PGF to "Progressive Total Return Fund, Inc." Contingent on the Merger not being consummated, CLM Stockholders are being asked to vote on

- Proposal 2 -- the re-election of Messrs. Ralph W. Bradshaw and Edwin Meese III to CLM's Board of Directors
- Proposal 3 -- the ratification of the selection of Tait, Weller & Baker as CLM's independent accountants for the year ending December 31, 2002; and
- Proposal 4-- a shareholder proposal requesting that CLM be converted to an open-end fund.

QUORUM

The presence, either in person or by proxy, of the holders of one-third of the outstanding shares of common stock entitled to vote at a meeting of either Fund, will constitute a quorum for the transaction of business by that Fund. For purposes of determining the presence of a quorum for transacting business at a meeting, abstentions and broker "non-votes" will be treated as shares that are present. Broker non-votes are proxies received by a Fund from brokers or nominees, indicating that the broker or nominee has neither received instructions from the beneficial owner or other persons entitled to vote nor has the discretionary power to vote on a particular matter. Stockholders are urged to forward their voting instructions promptly.

REQUIRED VOTE

Proposal 1, to be submitted at the PGF and CLM Meetings, requires the affirmative vote of a majority of the outstanding shares of common stock of each Fund.

PGF Proposal 2, to be submitted at the PGF Special Meeting, requires the affirmative vote of a majority of the outstanding shares of common stock of PGF.

CLM Proposals 2, 3 and 4, to be submitted at the CLM Annual Meeting, requires the affirmative vote of a majority of the votes cast at the meeting.

Abstentions and broker non-votes will have the effect of a "no" vote for Proposal 1, and PGF Proposal 2, and will have no effect on CLM's Proposal 2, 3 and 4.

Proxy solicitations will be made primarily by mail, but solicitations may also be made by telephone, telegraph or personal interviews conducted by officers or employees of the Funds, Cornerstone Advisors, Inc., the investment adviser to each of the Funds (the "Investment Adviser"), Bear Stearns Funds Management Inc., the administrator to each of the Funds (the "Administrator"), and Georgeson Shareholder Communication, Inc., a proxy solicitation firm ("Georgeson"). The Funds will bear their respective costs of solicitation.

An agreement between the Funds and Georgeson provides for Georgeson to provide general solicitation services to the Funds at an aggregate estimated cost of $14,000, including expenses. The Funds will, upon request, bear the reasonable expenses of brokers, bank and their nominees who are holders of record of the Funds' voting securities on the record date, incurred in mailing copies of this Proxy Statement/Prospectus to the beneficial owners of the Funds' voting securities.

Only stockholders of record of each Fund at the close of business on September 6, 2002 (the "Record Date"), are entitled to vote. An outstanding share of each Fund is entitled to one vote on all matters voted upon at a meeting of the stockholders of that Fund. As of September 6, 2002, there were 1,151,132 shares of PGF outstanding, and 3,813,264 shares of CLM outstanding.

PGF and CLM provide periodic reports to all of their stockholders. These reports highlight relevant information including investment results and a review of portfolio changes for each Fund. You may receive a copy of the most recent annual and semi-annual reports for PGF or CLM, without charge, by calling (212) 272-2093 or 1-866-227-3400, or writing to the Secretary of the Fund c/o Bear Stearns Funds Management Inc. located at 383 Madison Avenue, 23rd Floor, New York, New York 10179.

The Boards of Directors of the Funds know of no business other than the proposals described above which will be presented for consideration at each Fund's respective Meeting. If any other matter is properly presented, it is the intention of the persons named in the enclosed proxy to vote on that matter in their discretion.

I. MERGER PROPOSAL TO BE VOTED ON BY STOCKHOLDERS OF PGF AND CLM.

PROPOSAL 1:

APPROVAL OF THE MERGER AGREEMENT AND PLAN
OF REORGANIZATION (THE "PLAN")

On August 2, 2002, the Boards of Directors of both Funds, including a majority of the Directors who are not "interested persons" (the "Non-interested Directors"), unanimously:

(1) declared that the merger of CLM with and into PGF is in the best interest of the Funds and the stockholders,
(2) declared that in their respective opinions neither Fund's existing stockholders will be diluted as a result of the Merger;
(3) approved the Plan, and
(4) recommended that the stockholders of each Fund approve the Plan.

Stockholders should note that the Board of Directors of the Funds are identical, therefore, the Non-interested Directors are "non-interested" with respect to each Fund and may not be considered to be at arms length with respect to the proposed Merger. The Board of Directors of each Fund suggests that stockholders carefully review the information contained in the Proxy Statement/Prospectus before casting a vote.

For more information about the merger, see "Information about the Merger."

The Plan is subject to the approval of the stockholders of both Funds and certain other conditions. It provides for the merger (the "Merger") of CLM with and into PGF in accordance with the Maryland General Corporation Law (the "MGCL"). As a result of the Merger:

- CLM will no longer exist,
- PGF will be the surviving corporation, and
- each share of common stock of CLM will convert into an equivalent dollar amount of full shares and fractional shares of common stock of PGF to all CLM stockholders that participate in CLM's dividend reinvestment plan, based on the net asset value per share of each Fund calculated at the close of business on the business day preceding the Effective Date. A "Business Day" is any day on which the NYSE is open for trading, and
- CLM stockholders that do not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares.

A copy of the Plan is attached to this Proxy Statement/Prospectus as Exhibit A, and the description of the Plan included in this Prospectus/Proxy Statement is qualified in its entirety by reference to Exhibit A.

The following provides a more detailed discussion about the Merger, each Fund and additional information that you may find helpful in deciding how to vote on the Merger.

SYNOPSIS

This summary highlights important information included in this Proxy Statement/Prospectus. This summary is qualified by reference to the more complete information included elsewhere in this Proxy Statement/Prospectus and the Plan. Stockholders of each Fund should read this entire Proxy Statement/Prospectus carefully.

THE PROPOSED MERGER.

The Boards of Directors of PGF and CLM, including the Non-interested Directors of each Fund, have unanimously approved the Plan. The Plan provides for the merger of CLM with and into PGF. As a result of the Merger:

- each share of common stock of CLM will convert into an equivalent dollar amount of full shares and fractional shares of PGF common stock will be issued to all CLM stockholders that participate in CLM's dividend reinvestment plan, based on the net asset value per share of each Fund calculated at the close of business on the business day preceding the Effective Date. A "Business Day" is any day on which the NYSE is open for trading;

- CLM stockholders that do not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares; and

- each stockholder of CLM participating in the dividend reinvestment plan will become a stockholder of PGF and will receive, on the Effective Date, that number of full and fractional shares of common stock of PGF having an aggregate net asset value equal to the aggregate net asset value of such stockholder's shares held in CLM as of the close of business on the Business Day preceding the Effective Date.

If the Merger is not consummated, each Fund will continue as a separate investment company, and the Board of Directors of each Fund will consider such other alternatives as it determines to be in the best interests of its stockholders.

FORM OF ORGANIZATION.

PGF is a closed-end, non-diversified management investment company and CLM is a closed-end, diversified management investment company, both of which are registered under the Investment Company Act. PGF and CLM were both organized as Maryland corporations in 1989 and 1987, respectively. Each Fund's Board of Directors is responsible for the management of the business and affairs of each Fund.

INVESTMENT OBJECTIVES.

PGF seeks total return consisting of capital appreciation and current income by investing primarily in U.S. and non-U.S. equity and debt securities.

CLM's investment objective is to seek long-term capital appreciation through investment in equity securities of U.S. and non-U.S. companies.

Each Fund's investment objectives are fundamental, and can only be changed with the approval of the holders of a `majority of its outstanding voting securities' as defined under the Investment Company Act.

The preceding summary of each Fund's investment objectives and certain policies should be considered in conjunction with the discussion below under "Risk Factors and Special Considerations" and "Comparison of Investment Objectives and Policies."

NET ASSETS OF THE FUNDS

At June 30, 2002, PGF had net assets of $28,464,996 and CLM had net assets of $29,413,776.

FEES AND EXPENSES--PGF AND CLM

Cornerstone Advisors, Inc. ("Cornerstone Advisors" or "Advisor"), has served as both PGF's and CLM's investment adviser since April 19, 2001. The agreements between the Advisor and each Fund are substantially identical. As compensation for its advisory services, Cornerstone Advisors is contractually entitled to receive from each Fund an annual fee of one percent (1%) of that Fund's average weekly net assets payable monthly. On June 19, 2002, Cornerstone Advisors implemented a voluntary fee waiver to begin on July 1, 2002, with regard to both funds, under which the Advisor voluntarily waives its management fees to each Fund to the extent that each Fund's monthly operating expenses exceed 0.10% of net assets. The voluntary fee waiver may be changed or discontinued at any time after December 31, 2002 in the discretion of the Advisor. The voluntary fee waiver will not, however, be affected by the Merger.

For the period April 19, 2001 through December 31, 2001, Cornerstone Advisors earned $331,733 for performing its advisory services to PGF. For the same period, Cornerstone Advisers earned $276,913 for advisory services performed for CLM. For the period beginning on January 1, 2001 and ending on

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March 31, 2001, Clemente Capital, Inc. acted as CLM's investment adviser and Wilmington Trust Co. acted as CLM's investment sub-adviser. Clemente Capital, Inc. was paid $78,665 and Wilmington Trust Co. was paid $26,222 as compensation for their respective services rendered to CLM for that period.

Bear Stearns Funds Management Inc. ("BSFM"), serves as PGF's and CLM's administrator. PGF and CLM each pay BSFM a monthly fee that is computed weekly at an annual rate of 0.10% of the respective Fund's average weekly net assets, subject to a minimum annual fee of $50,000. In addition to the fee, each Fund is required to reimburse the Administrator all out-of-pocket expenses incurred by the Administrator for attendance at any meetings (outside the New York metropolitan area) of the Board of Directors, or any committees of such Board, or any other meetings or presentations for which the Administrator is

required to attend. For the period January 1, 2001 through December 31, 2001, BSFM earned $58,976 for services performed on behalf of PGF. For the period April 19, 2001 through December 31, 2001, BSFM earned $39,658 for services performed on behalf of CLM. Prior to BSFM becoming the administrator to CLM, PFPC, Inc. acted as CLM's administrator. During the period beginning January 1, 2001 and ending April 19, 2001, PFPC, Inc. earned $21,696 for its services rendered on behalf of CLM.

Based on June 30, 2002 net assets and projected expenses for the year 2002, in the absence of a voluntary fee waiver, PGF's annualized expense ratio would be expected to be approximately 2.35% Based on similar assumptions, PGF's annualized expense ratio after the Merger, not including the expenses of the Merger, is projected to be approximately 1.71%. So long as the voluntary fee waiver described above is in effect, PGF's annualized expense ratio, including the expenses of the merger, is expected to be 1.20%. The actual expense ratios for the current and fiscal years, whether or not the Merger occurs, may be higher or lower than these projections and depend upon performance, general stock market and economic conditions, net asset levels, stock prices and other factors, as well as whether the voluntary fee waiver is continued.

See "Expense Table" for the current expenses of each Fund and pro forma expenses following the Merger.

DISTRIBUTION POLICIES

In June 2002 both Funds announced distribution policies under which they would distribute fixed, monthly amounts. Such amounts have been distributed in July and August and distributions have been declared by the Boards of Directors for the month of September. Such distributions may be treated as returns of capital, capital gain or ordinary income depending on each Fund's tax position for the year as a whole. Stockholders will be advised of the relevant treatment when the tax positions are known.

It is the intention of the current Board of Directors to continue its current distribution policy after the Merger but there can be no guarantee that the policy will be continued for any specific time period.

UNREALIZED CAPITAL GAINS/LOSSES.

As of June 30, 2002, PGF had approximately $5,950,000 of unrealized capital losses, representing approximately 20.90% of its net assets. As of that same date, CLM had approximately $515,000 of unrealized capital gains, representing approximately 1.75% of its net assets. As of December 31, 2001, PGF and CLM had $11,780,944 and $142,060 of capital loss carryforwards, respectively.

FEDERAL INCOME TAX CONSEQUENCES OF THE MERGER.

As a condition to the closing of the Merger, both Funds will receive an opinion of Spitzer & Feldman P.C., counsel to the Funds, stating that the Merger will constitute a tax-free reorganization within the meaning of Section 368(a)(1) of the Internal Revenue Code of 1986 (the "Code"). Accordingly, neither CLM, PGF nor the stockholders of either Fund will recognize any substantial gain or loss as a result of the Merger. The holding period and the aggregate tax basis of PGF shares received by a CLM stockholder will be the same

as the holding period and aggregate tax basis of the shares of CLM previously held by the stockholder. All the CLM stockholders that do not participate in CLM's dividend reinvestment plan and receive cash for their fractional shares may recognize gain. The holding period and the aggregate tax basis of the assets received by PGF in the Merger will be the same as the holding period and the tax basis of such assets in the hands of CLM immediately before the Merger. For more information about the tax consequences of the Merger, see "Information about the Merger - Tax Considerations."

DISCOUNT FROM NET ASSET VALUE.

Shares of closed-end funds frequently trade at a market price that is less than the value of a fund's net assets. The possibility that shares of PGF and CLM will trade at a discount from its net asset value is a risk separate and distinct from the risk that such Fund's net asset value will decrease. Except for limited periods of time, PGF's and CLM's shares have traded in the market at a discount.

EXPENSES OF THE MERGER.

In evaluating the proposed Merger, Cornerstone Advisors has estimated the amount of expenses the Funds would incur at approximately $137,000, which includes NYSE fees, SEC registration fees, legal and accounting fees, proxy and distribution costs, and expenses incurred in connection with the Merger. The aggregate amount of estimated expenses of the Merger will be allocated equally between the Funds, regardless of whether the Merger is consummated, including the SEC registration fees and the fees for listing additional shares of PGF on the NYSE.

The expenses of the Merger, without giving effect to the voluntary fee waiver, are expected to result in a reduction in net asset value per PGF share of approximately $0.06, and a reduction in net asset value per CLM share of approximately $0.02.

PRINCIPAL RISK FACTORS

Both PGF and CLM are closed-end management investment companies and are designed primarily for long-term investors and not as trading vehicles.

STOCK MARKET VOLATILITY. Stock markets can be volatile. In other words, the prices of stocks can rise or fall rapidly in response to developments affecting a specific company or industry, or to changing economic, political or market conditions. The Funds are subject to the general risk that the value of their investments may decline if the stock markets perform poorly. There is also a risk that each Fund's investments will underperform either the securities markets generally or particular segments of the securities markets.

ISSUER SPECIFIC CHANGES. Changes in the financial condition of an issuer, changes in the specific economic or political conditions that affect a particular type of security or issuer, and changes in general economic or political conditions can affect the credit quality or value of an issuer's securities. Lower-quality debt securities tend to be more sensitive to these changes than higher-quality debt securities.

INTEREST RATE RISK. Debt securities have varying levels of sensitivity to changes in interest rates. In general, the price of a debt

security can fall when interest rates rise and can rise when interest rates fall. Securities with longer maturities and mortgage securities can be more sensitive to interest rate changes although they usually offer higher yields to compensate investors for the greater risks. The longer the maturity of the security, the greater the impact a change in interest rates could have on the security's price. In addition, short-term and long-term interest rates do not necessarily move in the same amount or the same direction. Short-term securities tend to react to changes in short-term interest rates and long-term securities tend to react to changes in long-term interest rates.

CREDIT RISKS. Fixed income securities rated B or below by S&Ps or Moody's may be purchased by either Fund. These securities have speculative characteristics and changes in economic conditions or other circumstances are more likely to lead to a weakened capacity of those issuers to make principal or interest payments, as compared to issuers of more highly rated securities.

EXTENSION RISK. Each Fund is subject to the risk that an issuer will exercise its right to pay principal on an obligation held by that Fund (such as mortgage-backed securities) later than expected. This may happen when there is a rise in interest rates. These events may lengthen the duration (i.e. interest rate sensitivity) and potentially reduce the value of these securities.

ILLIQUID SECURITIES.Each Fund may invest up to 15% of its respective net assets in illiquid securities. Illiquid securities may offer a higher yield than securities which are more readily marketable, but they may not always be marketable on advantageous terms. The sale of illiquid securities often requires

more time and results in higher brokerage charges or dealer discounts than does the sale of securities eligible for trading on national securities exchanges or in the over-the-counter markets. A security traded in the U.S. that is not registered under the Securities Act will not be considered illiquid if Fund management determines that an adequate investment trading market exists for that security. However, there can be no assurance that a liquid market will exist for any security at a particular time.

INVESTMENT IN SMALL AND MID-CAPITALIZATION COMPANIES. Each Fund may invest in companies with mid or small sized capital structures (generally a market capitalization of $5 billion or less). Accordingly, the Fund may be subject to the additional risks associated with investment in these companies. The market prices of the securities of such companies tend to be more volatile than those of larger companies. Further, these securities tend to trade at a lower volume than those of larger more established companies. If a Fund is heavily invested in these securities and the value of these securities suddenly declines, that Fund will be susceptible to significant losses.

OVER-THE-COUNTER BULLETIN BOARD MARKETS. Each Fund may invest in companies whose stock is trading on the over-the-counter Bulletin Board which have only a limited trading market. A more active trading market may never develop. Each Fund may be unable to sell its investments in these companies on any particular day due to the limited trading market.

ANTI-TAKEOVER PROVISIONS. Each Fund's Charter and Bylaws include provisions that could limit the ability of other persons or entities to acquire control of the Fund or to cause it to engage in certain transactions or to modify its structure.

LEVERAGE RISK. Utilization of leverage is a speculative investment technique and involves certain risks to the holders of common stock. These include the possibility of higher volatility of the net asset value of the common stock and potentially more volatility in the market value of the common stock. So long as each Fund is able to realize a higher net return on its investment portfolio than the then current cost of any leverage together with other related expenses, the effect of the leverage will be to cause holders of common stock to realize higher current net investment income than if the Fund were not so leveraged. On the other hand, to the extent that the then current cost of any leverage, together with other related expenses, approaches the net return on the Fund's investment portfolio, the benefit of leverage to holders of common stock will be reduced, and if the then current cost of any leverage were to exceed the net return on the Fund's portfolio, the Fund's leveraged capital structure would result in a lower rate of return to Common Shareholders than if the Fund were not so leveraged. There can be no assurance that each Fund's leverage strategy will be successful.

FOREIGN SECURITIES RISK. Investments in securities of non-U.S. issuers involve special risks not presented by investments in securities of U.S. issuers, including the following: less publicly available information about companies due to less rigorous disclosure or accounting standards or regulatory practices; the impact of political, social or diplomatic events; possible seizure, expropriation or nationalization of the company or its assets; and possible imposition of currency exchange controls. These risks are more pronounced to the extent that each Fund invests a significant amount of its investments in companies located in one region.

DEBT SECURITY RISK. In addition to interest rate risk, call risk and extension risk, debt securities are also subject to the risk that they may also lose value if the issuer fails to make principal or interest payments when due, or the credit quality of the issuer falls.

COMMON STOCK RISK. While common stock has historically generated higher average returns than fixed income securities, common stock has also experienced significantly more volatility in those returns. An adverse event, such as an unfavorable earnings report or acts of terrorism, may depress the value of common stock held by the Fund. Also, the price of common stock is sensitive to general movements in the stock market. A drop in the stock market may depress the price of common stock held by the Fund.

MARKET DISCOUNT FROM NET ASSET VALUE. Shares of closed end investment companies frequently trade at a discount from their net asset value. This characteristic is a risk separate and distinct from the risk that the Fund's net asset value could decrease as a result of its investment activities and may be greater for investors expecting to sell their shares in a relatively short period following completion of this offering. The net asset value of the common stock will be reduced immediately following the offering as a result of the payment of certain offering costs. Whether investors will realize gains or losses upon the sale of the common stock will depend not upon the Fund's net asset value but entirely upon whether the market price of the common stock at the time of sale is above or below the investor's purchase price for the common stock. Because the market price of the common stock will be determined by factors such as relative supply of and demand for the common stock in the market, general market and economic conditions, and other factors beyond the control of the Fund, the Fund cannot predict whether the common stocks will trade at, below or above net asset value or at, below or above the initial

public offering price. In recent years, shares of both Funds have traded at a discount to their respective net asset values.

NON-DIVERSIFICATION.Because PGF is classified as "non-diversified" under the Investment Company Act it can invest a greater portion of its assets in securities of a single issuer. As a result, PGF will be more susceptible than CLM, a more widely diversified fund, to any single corporate, economic, political or regulatory occurrence.

As a shareholder, you may pay certain fees and expenses if you hold shares of PGF, CLM or in PGF post merger. These fees and expenses, including based on a pro forma basis, post merger are set forth in the table below and the example that follows.

EXPENSE TABLE

SHAREHOLDER TRANSACTION EXPENSES	PGF	CLM	PGF PRO FORMA, POST MERGER
Sales Load (as a percentage of offering price)	N/A	N/A	N/A
Dividend Reinvestment and Cash Purchase Plan Fees	$0	$0	$0
ANNUAL EXPENSES(1)			
Investment Advisory Fees	1.00%	1.00%	1.00%
OTHER EXPENSES(2)	1.35%	1.17	0.71%
TOTAL ANNUAL EXPENSES	2.35%(3)	2.17%(3)	1.71%(3)

(1) The percentages in the above table expressing annual fund operating expenses are based on each Fund's operating expenses.

(2) Other Expenses include administration, fund accounting, custody and transfer agency fees as well as legal and auditing annual expenses. These figures do not reflect the expenses of the Merger.

(3) Total Annual Expenses do not reflect the effect of any voluntary fee waiver by the Adviser. Assuming that the voluntary fee waiver by the Adviser continues, the Total Annual Expenses are anticipated to be approximately 1.20%. Cornerstone Advisors has committed to voluntarily waive fees through December 31, 2002. The Adviser may discontinue the fee waiver after the date, in its sole discretion.

Example. The purpose of the following example is to help you understand the costs and expenses you may bear as an investor. This example is based on the level of total annual operating expenses for each Fund listed in the table above, the total expenses relating to a $10,000 investment, assuming a 5% annual return and reinvestment of all dividends and distributions. Stockholders do not pay these expenses directly, they are paid by the Funds before they distribute

net investment income to Stockholders. This example should not be considered a representation of future expenses, and actual expenses may be greater or less than those shown. Federal regulations require the example to assume a 5% annual return, but actual annual returns will vary.

	PGF	CLM	PGF PRO FORMA, POST MERGER
1 Year	$238	$220	$174
3 Years	$733	$679	$539
5 Years	$1,255	$1,164	$ 928
10 Years	$2,686	$2,503	$2,019

FINANCIAL HIGHLIGHTS

The information required in this portion is being incorporated by reference from each Fund's Semi-Annual Report to Stockholders Dated June 30, 2002 which have been filed with the Commission. Each Fund's Annual Report dated December 31, 2001 and Semi-Annual Report dated June 30, 2002 may be obtained without charge, by writing to the Secretary of the respective Fund c/o Bear Stearns Funds Management Inc., 383 Madison Avenue, 23 Fl., New York, New York 10179, or by calling (212) 272-2093.

COMPARISON OF INVESTMENT OBJECTIVES AND POLICIES

ORGANIZATION.

PGF is a closed-end, non-diversified management investment company and CLM is a closed-end, diversified management investment company, both registered under the Investment Company Act. Both Funds are organized as corporations under the laws of the State of Maryland. Each Fund is managed and advised by Cornerstone Advisors. The shares of common stock of each Fund are listed and trade on the NYSE under the symbols "PGF" and "CLM", respectively. After the Merger, PGF's shares will continue to trade on the NYSE under the symbol "PGF", while CLM's shares will be delisted and CLM will cease to exist.

The shares of common stock of each Fund have equal non-cumulative voting rights and equal rights with respect to dividends, assets and dissolution. Each Fund's shares of common stock are fully paid and non-assessable and have no preemptive, conversion or other subscription rights. Fluctuations in the market price of the Funds' shares is the principal investment risk of an investment in either Fund. Portfolio management, market conditions, investment policies and other factors affect such fluctuations. Although the investment objectives, policies and restrictions of the Funds are similar, there are differences between them, as discussed below. There can be no assurance that either Fund will achieve its stated objective.

INVESTMENT OBJECTIVES.

PGF

PGF's investment objective is to seek total return consisting of capital appreciation and current income by investing primarily in equity securities of U.S. and non-U.S. companies and U.S. dollar denominated debt

securities which Fund management believes have demonstrated fundamental investment value and favorable growth prospects. In general, PGF invests in such

equity securities that are traded in the United States on a securities exchange or over the counter or as sponsored American Depositary Receipts ("ADR") or other forms of depositary receipt, such as International Depositary Receipts ("IDR"). Depositary receipts, which are sponsored, are issued with the cooperation of the company whose stock underlies the ADR. They are traded over an exchange like common stocks in the United States, are typically issued in connection with a U.S. or foreign banks or trust companies and evidence ownership of the underlying securities issued by a foreign corporation including, voting rights.

CLM

CLM's investment objective is to seek long-term capital appreciation through investment primarily in equity securities of U.S. and non-U.S. companies which Fund management believes have demonstrated fundamental investment value and favorable growth prospects. In general, CLM invests primarily in common stocks, preferred stocks, rights, warrants and securities convertible into common stocks that are listed on stock exchanges or traded over the counter.

Each Fund's foregoing investment objective cannot be changed without the vote of a majority of that Fund's outstanding voting securities as defined in the Investment Company Act. No assurance can be given that either Fund's investment objective will be achieved.

COMPARISON OF PRINCIPAL INVESTMENT POLICIES.

PGF

PGF's portfolio, under normal market conditions, consists principally of the equity securities of large, mid and small-capitalization companies. Equity securities in which the Fund may invest include common and preferred stocks, convertible securities, warrants and other securities having the characteristics of common stocks, such as ADRs and IDRs. The Fund may, however, invest a portion of its assets in U.S. dollar denominated debt securities when Fund management believes that it is appropriate to do so in order to achieve the Fund's investment objective - for example when interest rates are high in comparison to anticipated returns on equity investments. Debt securities in which the Fund may invest include U.S. dollar denominated bank, corporate or government bonds, notes, and debentures of any maturity determined by Fund management to be suitable for investment by the Fund. The Fund may invest in the securities of issuers that it determines to be suitable for investment by the Fund regardless of their rating. The Fund may not, however, invest more than 5% of its assets in debt securities that are determined by Fund management to be rated or comparable to securities rated B or below by S&P or Moody's.

PGF's management utilizes a balanced approach, including value and growth investing by seeking out companies at reasonable prices, without regard to sector or industry, that demonstrate favorable long-term growth characteristics. Valuation and growth characteristics may be considered for purposes of selecting potential investment securities. In general in the

securities industry, valuation analysis is used to determine the inherent value of the company by analyzing financial information such as a company's price to book, price to sales, return on equity, and return on assets ratios and growth analysis is used to determine a company's potential for long-term dividends and earnings growth due to market-oriented factors such as growing market share, the launch of new products or services, the strength of its management and market demand.

PGF may also invest up to 10% of its assets in the aggregate in the securities of other investment companies and up to 5% of its assets in any one such investment company, provided that such investment does not represent more than 3% of the voting stock of the acquired investment company of which such shares are purchased. As a shareholder in any investment company, the Fund will bear its ratable share of the investment company's expenses and would remain subject to payment of the Fund's advisory and administrative fees with respect to the assets so invested.

PGF may invest up to 15% of its assets in illiquid U.S. and non-U.S. securities, provided that the Fund may not invest more than 3% of the Fund's assets in the securities of companies that, at the time of investment, had less than a year of operations, including operations of predecessor companies. The Fund will invest only in such illiquid securities that, in the opinion of Fund management, present opportunities for substantial growth over a period of two to five years.

PGF does not expect to trade in securities for short-term gains. Higher portfolio turnover rates resulting from more actively traded portfolio securities generally result in higher transaction costs, including brokerage commissions and related capital gains or losses. Since the Fund's investment policies emphasize long-term investment in the securities of companies, the Fund's annual portfolio turnover rate is expected to be relatively low, ranging between 50% and 75%.

CLM

CLM's portfolio, under normal market conditions, will consist principally of the equity securities of U.S. and non-U.S. companies. In general, CLM invests primarily in common stocks, preferred stocks, rights, warrants and securities convertible into common stocks that are listed on stock exchanges or traded over the counter. The Fund may, without limitation, hold cash or invest in assets in money market instruments, including U.S. and non-U.S. government securities, high grade commercial paper and certificates of deposit and bankers' acceptances issued by U.S. and non-U.S. banks having deposits of at least $500 million. In addition, CLM may engage in hedging transactions to reduce its company market and currency exchange exposure.

CLM may also invest up to 10% of its assets in the aggregate in the securities of other investment companies and up to 5% of its assets in any one such investment company, provided that such investment does not represent more than 3% of the voting stock of the acquired investment company of which such shares are purchased. As a shareholder in any investment company, the Fund will bear its ratable share of the investment company's expenses and would remain subject to payment of the Fund's advisory and administrative fees with respect to the assets so invested.

CLM may invest up to 15% of its assets in illiquid U.S. and non-U.S. securities, provided that the Fund may not invest more than 3% of the Fund's assets in the securities of companies that, at the time of investment, had less than a year of operations, including operations of predecessor companies. The Fund will invest only in such illiquid securities that, in the opinion of Fund management, present opportunities for substantial growth over a period of two to five years.

CLM does not expect to trade in securities for short-term gains. Higher portfolio turnover rates resulting from more actively traded portfolio securities generally result in higher transaction costs, including brokerage commissions and related capital gains or losses. Since the Fund's investment policies emphasize long-term investment in the securities of companies, the Fund's annual portfolio turnover rate is expected to be relatively low, ranging between 50% and 75%.

Although CLM has the ability to invest a significant portion of its assets in non-U.S. companies, the Fund has maintained the investment of at least 94% of its assets in U.S. companies during the period from June 30, 2001 through June 30, 2002.

Each Fund's foregoing investment policies may be changed by each Fund's respective Board of Directors without shareholder vote.

CLM'S AND PGF'S NON-PRINCIPAL INVESTMENT POLICIES

TEMPORARY DEFENSIVE POSITIONS. Each Fund may, in attempting to respond to adverse market, economic, political or other conditions, take temporary defensive positions that are inconsistent with its principal investment strategies. Such investments include various short-term instruments. If a Fund takes a temporary defensive position at the wrong time, the position would have an adverse impact on the Fund's performance and it may not achieve its investment objective.

SECURITIES LENDING. Each Fund may lend its portfolio securities to broker-dealers in amounts equal to no more than 33 1/3% of the Fund's net assets. These transactions will be fully collateralized at all times with cash and/or high quality, short-term debt obligations. These transactions involve risk to a Fund if the other party should default on its obligation and the Fund is delayed or prevented from recovering the securities lent. In the event the original borrower defaults on its obligation to return lent securities, the Fund will seek to sell the collateral, which could involve costs or delays. To the extent proceeds from the sale of collateral are less than the repurchase price, the Fund would suffer a loss and you could lose money on your investment.

BORROWING.Each Fund may borrow money from banks for temporary or emergency purposes or for the clearance of transactions in amounts not exceeding 10% (taken at the lower of cost or current value) of its total assets (not including the amount borrowed) and may also pledge its assets to secure such borrowings. To reduce its indebtedness, a Fund may have to sell a portion of its investments at a time when it may be disadvantageous to do so. In addition, interest paid by the Fund on borrowed funds would decrease the net earnings of the Fund.

REPURCHASE AGREEMENTS. Each Fund may enter into repurchase agreements collateralized by the securities in which it may invest. A repurchase agreement involves the purchase by the Fund of securities with the condition that the original seller (a bank or broker-dealer) will buy back the same securities (collateral) at a predetermined price or yield. Repurchase agreements involve certain risks not associated with direct investments in securities. In the event the original seller defaults on its obligation to repurchase, the Fund will seek to sell the collateral, which could involve costs or delays. To the extent proceeds from the sale of collateral are less than the repurchase price, the Fund would suffer a loss.

Under the Investment Company Act, neither Fund may:

- invest more than 5% of its total assets in the securities of any one investment company, nor
- acquire more than 3% of the outstanding voting securities of any such company.

UNITED STATES FEDERAL INCOME TAXES

The following is a brief summary of certain United States federal income tax issues that apply to each Fund. Stockholders should consult their own tax advisers with regard to the federal tax consequences of the purchase, ownership and disposition of each Fund's shares, as well as tax consequences arising under the laws of any state, foreign country, or other taxing jurisdiction.

Each Fund has qualified, and intends to continue to qualify and elect to be treated, as a regulated investment company ("RIC"), for each taxable year under Subchapter M of the Code. A RIC generally is not subject to federal income tax on income and gains distributed in a timely manner to its stockholders.

Each Fund intends to distribute annually to its stockholders substantially all of its investment company taxable income. The Board of Directors of each Fund will determine annually whether to distribute any net realized long-term capital gains in excess of net realized short-term capital losses, including any capital loss carryovers. The Funds currently expect to distribute any excess annually to their stockholders. However, if either Fund retains for investment an amount equal to its net long-term capital gains in excess of its net short-term capital losses and capital loss carryovers, it will be subject to a corporate tax, currently at a rate of 35%, on the amount retained. In that event, that Fund expects to designate such retained amounts as undistributed capital gains in a notice to its stockholders who:

- will be required to include in income for United States federal income tax purposes, as long-term capital gains, their proportionate shares of the undistributed amount,

- will be entitled to credit their proportionate shares of the 35% tax paid by that Fund on the undistributed amount against their United States federal income tax liabilities, if any, and to claim refunds to the extent their credits exceed their liabilities, if any, and

- will be entitled to increase their tax basis, for United States

federal income tax purposes, in their shares by an amount equal to 65% of the amount of undistributed capital gains included in the stockholder's income.

Income received by the Funds from sources within countries other than the United States may be subject to withholding and other taxes imposed by such countries, which will reduce the amount available for distribution to stockholders. If more than 50% of the value of either Fund's total assets at the close of its taxable year consists of securities of foreign corporations, that Fund will be eligible and intends to elect to "pass-through" to stockholders the amount of foreign income and similar taxes it has paid. Pursuant to this election, stockholders of the electing Fund will be required to include in gross income (in addition to the full amount of the taxable dividends actually received) their pro rata share of the foreign taxes paid by that Fund. Each such stockholder will also be entitled either to deduct (as an itemized deduction) its pro rata share of foreign taxes in computing its taxable income or to claim a foreign tax credit against its U.S. federal income tax liability, subject to limitations. No deduction for foreign taxes may be claimed by a stockholder who does not itemize deductions, but such a stockholder may be eligible to claim the foreign tax credit. The deduction for foreign taxes is not allowable in computing alternative minimum taxable income. Each stockholder will be notified within 60 days after the close of that Fund's taxable year whether the foreign taxes paid by the Fund will "pass through" for that year.

Generally, a credit for foreign taxes is subject to the limitation that it may not exceed the stockholder's U.S. tax attributable to his or her foreign source taxable income. For this purpose, if the pass-through election is made, the source of each Fund's income flows through to its stockholders. Any gains from the sale of securities by either Fund will be treated as derived from U.S. sources and certain currency fluctuation gains, including fluctuation gains from foreign currency-denominated debt securities, receivables and payables, will be treated as ordinary income derived from U.S. sources. The limitation on the foreign tax credit is applied separately to foreign source passive income (as defined for purposes of the foreign tax credit), including the foreign source passive income passed through by each Fund. Because of the limitation, stockholders taxable in the United States may be unable to claim a credit for the full amount of their proportionate share of the foreign taxes paid by each Fund. The foreign tax credit also cannot be used to offset more than 90% of the alternative minimum tax (as computed under the Code for purposes of this limitation) imposed on corporations and individuals.

Stockholders will be notified annually by each Fund as to the United States federal income tax status of the dividends, distributions and deemed distributions made by the Fund to its stockholders. Furthermore, stockholders will also receive, if appropriate, various written notices after the close of each Fund's taxable year regarding the United States federal income tax status of certain dividends, distributions and deemed distributions that were paid, or that are treated as having been paid, by that Fund to its stockholders during the preceding taxable year. For a more detailed discussion of tax matters affecting each Fund and its stockholders, see "Taxation" in the SAI.

INFORMATION ABOUT THE MERGER

GENERAL.

Under the Plan, CLM will merge with and into PGF on the Effective

Date. As a result of the Merger and on the Effective Date:

- CLM will no longer exist, and

- PGF will be the surviving corporation and CLM will then:

  1) deregister as an investment company under the Investment Company Act,
  2) withdraw from registration under the Securities Exchange Act of 1934 (the "Exchange Act"),
  3) remove its shares of common stock from listing on the NYSE, and
  4) cease its separate existence under Maryland law.

Each share of common stock of CLM will convert into an equivalent dollar amount of full shares of PGF common stock based on the net asset value per share of each Fund calculated at the close of business on the Business Day preceding the Effective Date. PGF fractional shares will be issued to all of the CLM stockholders that participate in CLM's dividend reinvestment plan. Any CLM stockholder that does not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares.

Under Section 3-202 of the Maryland General Corporation Law, stockholders of a corporation whose shares are traded publicly on a national securities exchange, such as the Funds' shares, are not entitled to demand the fair value of their shares upon a merger; therefore, the stockholders of the Funds will be bound by the terms of the Merger. However, any stockholder of either Fund may sell his or her shares of common stock at any time prior to the Merger on the NYSE.

The Plan may be terminated and the Merger abandoned, whether before or after approval by the Funds' stockholders, at any time prior to the Effective Date:

- by the mutual written consent of the Board of Directors of each Fund, or

- by either Fund if the conditions to that Fund's obligations under the Plan have not been satisfied or waived.

If the Merger has not been consummated by December 31, 2002, the Plan automatically terminates on that date, unless a later date is mutually agreed upon by the Board of Directors of each Fund.

REASONS FOR THE MERGER.

The Board of Directors of each Fund considered and unanimously approved the proposed Merger at separate meetings of each Board held on August 2, 2002. For the reasons discussed below, the Board of Directors of each Fund, including Non-interested Directors of each Fund, after consideration of the potential benefits of the Merger to the stockholders of that Fund and the expenses expected to be incurred by that Fund in connection with the Merger, unanimously determined that:

- the interests of the existing stockholders of that Fund will not be diluted as a result of the proposed Merger, and

- the proposed Merger is in the best interests of that Fund.

The reasons stated above were fully recorded in each Fund's minute books.

Three principal factors led each Fund's Board of Directors to reach these conclusions: (1) the Merger will create a larger Fund and, consequently, should, all other factors being equal, result in an expense ratio that is lower than the expense ratio of either Fund; (2) the larger Fund should provide better market liquidity for stockholders who want to sell their shares or add to their holdings; and (3) it has been a prime objective of each Board, through a variety of actions, to reduce the discount at which shares trade. Some of the actions taken to reduce the discount include the implementation of several large distributions to PGF's stockholders which the Adviser believes will be classified as a return of capital, a one-for-four reverse stock split that was recently completed, and, as of June 30, 2002, PGF's Board implemented a fixed, monthly distribution policy. Some of the actions taken by CLM's Board of Directors include the implementation of an aggressive buy-back program and the implementation of a fixed, monthly distribution policy. In addition to those actions taken, the investment Adviser of both Fund's agreed to implement a voluntary fee waiver. Thus, the Adviser will voluntarily waive its management fees to each Fund to the extent that monthly operating expenses exceed 0.10% of net assets calculated on a monthly basis. The Boards believe that, all other things being equal, a lower expense ratio and better market liquidity for the shares should lead to a lower discount.

IN THE JUDGMENT OF THE BOARD OF DIRECTORS OF EACH FUND, THE MERGER SERVES THE BEST INTERESTS OF EACH FUND AND ITS STOCKHOLDERS.

Stockholders should note that the Boards of Directors of the two Funds are identical. Therefore, although the Non-interested Directors are "non-interested" with respect to each of the Funds under the Investment Company Act, they are not at arm's length with respect to the proposed Merger.

The Board of Directors of each Fund, in declaring advisable and recommending the proposed Merger, also considered the following:

(1) the capabilities and resources of Cornerstone Advisors in the area of investment management;
(2) expense ratios and information regarding fees and expenses of the Funds, both currently and on a pro forma basis;
(3) the terms and conditions of the Merger and whether it would result in dilution of the interests of each Fund and its existing stockholders;
(4) the compatibility of each Fund's portfolio securities, investment objective, policies and restrictions;
(5) the tax consequences to each Fund and its stockholders in connection with the Merger; and
(6) the anticipated expenses of the Merger.

In reviewing issues relating to the structure of the Merger and the selection of the surviving corporation in the Merger, each Board also considered

information provided to them by Cornerstone Advisors concerning:

(1) the comparative performance records of the two Funds,
(2) public and market perception of the two Funds,
(3) the relative size of the two Funds,
(4) the investment policies and strategies Cornerstone Advisors intends to utilize in managing the merged fund,
(5) Cornerstone Advisors' recommendation that PGF be the surviving corporation, and
(6) the relative tax positions of the Funds.

TERMS OF THE MERGER AGREEMENT.

The following is a summary of the significant terms of the Plan. This summary is qualified in its entirety by reference to the Plan, attached hereto as Exhibit A.

Each share of common stock of CLM will convert into an equivalent dollar amount of full shares of PGF common stock based on the net asset value per share of each Fund calculated at the close of business on the Business Day (as defined in the Plan of Merger) preceding the Effective Date. PGF fractional shares will be issued to all of the CLM stockholders that participate in CLM's dividend reinvestment plan. Any CLM stockholder that does not participate in CLM's dividend reinvestment plan will not receive fractional shares, rather PGF's transfer agent will aggregate all fractional shares, sell the resulting full shares on the New York Stock Exchange at the then current market price and remit the proceeds to CLM's stockholders in proportion to their fractional shares.

For purposes of valuing assets in connection with the Merger, the assets of CLM will be valued pursuant to the principles and procedures consistently utilized by PGF, which principles and procedures are also utilized by CLM in valuing its own assets and determining its own liabilities. As a result, it is not expected that PGF's valuation procedures as applied to CLM's portfolio securities will result in any difference from the valuation that would have resulted from the application of CLM's valuation procedures to such securities. The net asset value per share of PGF common stock will be determined in accordance with these principles and procedures, and PGF will certify the computations involved. The net asset value per share of each Fund will not be adjusted to take into account differences in unrealized gains and losses, nor will it be adjusted to take into account the potential value of capital loss carryforwards.

PGF will issue separate certificates or share deposit receipts for PGF common stock to stockholders of CLM. PGF will deliver these certificates or share deposit receipts representing shares of PGF common stock to American Stock Transfer & Trust Co., as the transfer agent and registrar for PGF common stock. PGF will not permit any CLM stockholder to receive new certificates representing shares of PGF common stock until the stockholder has surrendered his or her outstanding certificates representing shares of the common stock of CLM or, in the event of lost certificates, posted adequate bond. CLM will request its stockholders to surrender their outstanding certificates representing shares of the common stock of CLM or post adequate bond therefor. Dividends payable to holders of record of shares of PGF as of any date after the Effective Date and prior to the exchange of certificates by any stockholder of CLM will be paid to

such stockholder, without interest; however, such dividends will not be paid unless and until such stockholder surrenders his or her stock certificates of CLM for exchange.

PLEASE DO NOT SEND IN ANY STOCK CERTIFICATES AT THIS TIME. UPON CONSUMMATION OF THE MERGER, STOCKHOLDERS OF CLM WILL BE FURNISHED WITH INSTRUCTIONS FOR EXCHANGING THEIR STOCK CERTIFICATES FOR PGF STOCK CERTIFICATES.

The net asset value of the PGF shares received by CLM stockholders will be equal to the aggregate net asset value of the CLM shares exchanged.

The Plan provides, among other things, that the Merger will not take place without:

- the requisite approval of the stockholders of PGF and CLM, and
- the effectiveness of a Registration Statement on Form N-14.

The Plan may be terminated at any time prior to the Effective Date by mutual agreement of each Fund's Board of Directors or by either Fund if the other has violated a condition of the Plan. The Plan will automatically terminate after December 31, 2002 if the Merger has not been consummated, unless such time is extended by mutual agreement of the Board of Directors of each Fund.

The Plan may be amended, modified or supplemented by mutual agreement of CLM and PGF. However, no amendments which would have the effect of changing the provisions for determining the number of shares issued to CLM stockholders will be permitted following the meeting unless those stockholders consent to the amendment.

EXPENSES OF THE MERGER.

In evaluating the proposed Merger, Cornerstone Advisors has estimated the amount of expenses the Funds will incur, including, but not limited to, NYSE listing fees, SEC registration fees, legal and accounting fees, proxy and distribution costs, and expenses incurred in connection with the Merger. The estimated total expenses pertaining to the Merger is approximately $137,000.

The expenses of the Merger, without giving effect to the voluntary fee waiver, are expected to result in a reduction in net asset value per PGF share of approximately $0.06, and a reduction in net asset value per CLM share of approximately $0.02.

TAX CONSIDERATIONS.

The Plan and Merger are conditioned upon the receipt by the Funds of an opinion from Spitzer & Feldman P.C., substantially to the effect that, based upon the facts, assumptions and representations of the parties, for federal income tax purposes:

- the Merger will constitute a tax-free "reorganization" within the meaning of Section 368(a)(1) of the Code, and each Fund will be "a party to a reorganization" within the meaning of Section 368(b) of the Code,

- no gain or loss will be recognized by either Fund as a result of the Merger,

- the basis of the assets of CLM in the hands of PGF will be the same as the basis of such assets to CLM immediately prior to the Merger,

- the holding period of the assets of CLM in the hands of PGF will include the period during which such assets were held by CLM,

- no gain or loss will be recognized by the stockholders of CLM upon the conversion of their CLM shares into PGF common stock,

- the basis of PGF shares received by the stockholders of CLM will be the same as the basis of the shares of CLM exchanged therefor,

- gain or loss may be recognized by the stockholders of CLM upon the issuance of cash in lieu of their fractional shares, and

- the holding period of PGF shares received by the stockholders of CLM will include the holding period during which the shares of CLM exchanged therefor were held, provided that at the time of the exchange the shares of CLM were held as capital assets in the hands of the stockholders of CLM.

While CLM is not aware of any adverse state or local tax consequences of the proposed Merger, it has not requested any ruling or opinion with respect to such consequences and stockholders may wish to consult their own tax advisers with respect to such matters.

The Board of Directors of each Fund considered the tax loss carryforward and current capital loss positions of the two Funds as part of their overall process of considering the proposed Merger. They also considered professional advice that they received regarding the future use of these various capital loss categories to offset future capital gains. This professional advice included the possibility that in some circumstances utilization of the capital loss carryforwards might be restricted, in part because of the Merger. The Boards also considered whether the ability to continue to utilize the capital loss carryforwards should be made a condition to the effectiveness of the Merger and concluded that it should not. The Boards concluded that in their respective judgments, under all of the facts and circumstances known to them after considering the advice of their professional advisers, the Merger is in the best interests of both Funds and their stockholders, even if as a consequence there may be "truncation" (restriction on the utilization) of the capital loss carryforwards under the Code.

ADDITIONAL INFORMATION ABOUT THE FUNDS

DESCRIPTION OF SECURITIES TO BE ISSUED.

The authorized stock of PGF consists of One Hundred Million (100,000,000) shares of common stock, U.S. $0.001 par value. Shares of PGF entitle its holders to one vote per share. Holders of PGF's common stock are entitled to share equally in dividends authorized by the Fund's Board of Directors payable to the holders of such common stock and in the net assets of PGF available for distribution to holders of such common stock. Shares have noncumulative voting rights and no conversion, preemptive or other subscription rights, and are not redeemable. The outstanding shares of common stock of PGF are fully paid and non-assessable. In the event of liquidation, each share of

common stock is entitled to its proportion of the Fund's assets after payment of debts and expenses. PGF holds stockholder meetings annually.

The following table shows information about the common stock of each Fund as of June 30, 2002.

	AMOUNT AUTHORIZED	AMOUNT HELD BY FUND	AMOUNT OUTSTANDING
PGF			
COMMON STOCK	100,000,000	0	1,147,786
CLM			
COMMON STOCK	25,000,000	2,204,140	3,805,860

As of June 30, 2002, the net asset value of PGF common stock was $24.80, and the market price per share was $23.40. As of that same date, the net asset value of CLM common stock was $7.73, and the market price per share was $6.65.

DISCOUNT TO NET ASSET VALUE.

Shares of closed-end investment companies, such as the Funds, have frequently traded at a discount from net asset value. This characteristic is a risk separate and distinct from the risk that the Funds' net asset values may decrease, and this risk may be greater for stockholders expecting to sell their shares in a relatively short period. THE SHARES OF COMMON STOCK OF THE FUNDS SHOULD THUS BE VIEWED AS BEING DESIGNED PRIMARILY FOR LONG-TERM INVESTORS AND SHOULD NOT BE CONSIDERED A VEHICLE FOR TRADING PURPOSES.

During the period since the inception of the Funds, the common stock of both Funds has generally traded at a discount to net asset value, and does so currently. It is not possible to state whether shares of PGF will trade at a premium or discount to net asset value following the Merger, or the extent of any such premium or discount. The Directors of both Funds have regularly considered, and the Directors of PGF will continue to consider, the respective Fund's market price discount and the effect of the discount on the Fund and its stockholders.

PER SHARE DATA FOR PROGRESSIVE RETURN FUND, INC.
COMMON STOCK TRADED ON THE NYSE

Quarter Ended	High Price ($)	Low Price ($)	Closing Market Price ($)	Closing Net Asset Value ($)
3/31/99	68.00	54.75	54.75	65.52
6/30/99	58.00	54.50	57.25	60.84
9/30/99	57.75	50.75	50.75	56.56
12/31/99	54.50	47.75	52.25	61.84

3/31/00	57.75	52.25	56.75	64.40
6/30/00	56.75	46.25	49.75	60.44
9/30/00	49.75	44.00	44.00	55.00
12/31/00	40.75	37.25	38.00	49.48
3/31/01	43.80	36.04	37.04	44.04
6/30/01	40.60	36.48	40.00	45.96
9/30/01	38.92	30.60	32.00	39.44
12/31/01	38.60	32.88	36.20	40.08
3/31/02	37.40	27.80	28.04	30.96
6/30/02	27.60	23.35	23.40	24.80

PER SHARE DATA FOR CORNERSTONE STRATEGIC VALUE FUND, INC.
COMMON STOCK TRADED ON THE NYSE

Quarter Ended	High Price ($)	Low Price ($)	Closing Market Price ($)	Closing Net Asset Value ($)
3/31/99	13.63	12.88	13.13	14.55
6/30/99	13.81	12.25	13.81	15.38
9/30/99	15.00	13.56	13.81	15.23
12/31/99	17.00	13.56	14.25	14.95
3/31/00	14.50	12.25	14.50	15.85
6/30/00	14.50	12.06	13.00	15.28
9/30/00	13.13	11.88	12.06	13.72
12/31/00	11.88	10.25	10.59	11.31
3/31/01	10.59	7.40	7.75	9.19
6/30/01	8.55	7.60	8.35	9.68
9/30/01	8.00	6.26	6.40	8.35
12/31/01	7.93	6.64	7.75	9.31
3/31/02	8.01	7.60	7.65	9.04
6/30/02	7.66	6.65	6.65	7.73

CAPITALIZATION.

The following table shows on an unaudited basis the capitalization of PGF and CLM as of June 30, 2002 and on a pro forma basis as of that same date giving effect to the Merger:

	PGF	CLM	PGF PRO FORMA POST MERGER
Net Assets	$28,464,996	$29,413,776	$57,708,555*
Shares of Common Stock Outstanding	1,147,786	3,805,860	2,332,779
Net Assets Per Share of Common Stock	$24.80	$7.73	$24.74

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* The Pro Forma Net Assets of PGF Post Merger account for the aggregate cost of the merger to both CLM and PGF, which is approximately $137,000.

DIVIDENDS AND OTHER DISTRIBUTIONS.

Each Fund intends to distribute dividends from its net investment income and any net realized capital gains after utilization of capital loss carryforwards annually to prevent application of a federal excise tax. An additional distribution may be made if necessary. Any dividends or capital gains distributions declared in October, November or December with a record date in such a month and paid during the following January will be treated by stockholders for federal income tax purposes as if received on December 31 of the calendar year in which it is declared. Dividends and distributions of each Fund are invested in shares of the Fund at market value and credited to the stockholder's account on the settlement date which is usually three Business Days from the purchase date or, at the stockholder's election, paid in cash.

On June 19, 2002, each Fund's Board of Directors authorized the implementation of a fixed, monthly distribution policy whereby PGF would distribute on a monthly basis $0.2675 per share and CLM would distribute $0.0825 per share to their respective stockholders. Each distribution could consist of either income, capital gains, or return of capital, or a combination of all three. The Board of Directors of PGF, in its continuing discretion, intends to continue a fixed, monthly distribution policy after the Merger.

PORTFOLIO VALUATION.

Investments of each Fund are stated at value in each Fund's financial statements. All securities for which market quotations are readily available are valued at the last sales price or lacking any sales, at the closing price last quoted for the securities (but if bid and asked quotations are available, at the mean between the current bid and asked prices). Securities that are traded over-the-counter are valued at the mean between the current bid and the asked prices, if available. All other securities and assets are valued at fair value as determined in good faith by each Fund's Board of Directors. Short-term investments having a maturity of 60 days or less are valued on the basis of amortized cost. The Board of Directors of each Fund has established general guidelines for calculating fair value of securities that are not readily marketable. At June 30, 2002, both PGF and CLM held no securities valued in good faith by the Board of Directors. The net asset value per share of each Fund is made public weekly.

For purposes of valuing assets in connection with the Merger, the assets of CLM will be valued pursuant to the principles and procedures consistently utilized by PGF, which principles and procedures are also utilized by CLM in valuing its own assets and determining its own liabilities. As a result, it is not expected that PGF's valuation procedures as applied to CLM's portfolio securities will result in any difference from the valuation that would have resulted from the application of CLM's valuation procedures to such securities.

DIVIDEND REINVESTMENT AND CASH PURCHASE PLAN.

Each Fund operates a Dividend Reinvestment and Cash Purchase Plan (the "Program"), sponsored and administered by American Stock Transfer & Trust Co. (the "Agent"), pursuant to which Fund dividends and distributions, net of any applicable U.S. withholding tax, are reinvested in shares of the Fund. American Stock Transfer & Trust Co., serves as the Program Administrator for the stockholders in administering the Program.

Stockholders who have shares registered directly in their own names automatically participate in the respective Fund's Program, unless and until an election is made to withdraw from the Program on behalf of such participating stockholder. Stockholders who do not wish to have distributions automatically reinvested should so notify the Agent at 59 Maiden Lane, New York, New York 10038. Under the Program, each of the Fund's respective dividends and other distributions to stockholders are reinvested in full and fractional shares as described below.

When the respective Fund declares an income dividend or a capital gain or other distribution (each, a "Dividend" and collectively, "Dividends"), the Agent, on the stockholders behalf, will (i) receive additional authorized shares from the respective Fund either newly issued or repurchased from stockholders by the Fund and held as treasury stock ("Newly Issued Shares") or, (ii) at the sole discretion of the Board of Directors, be authorized to purchase outstanding shares on the open market, on the NYSE or elsewhere, with cash allocated to it by the respective Fund ("Open Market Purchases").

Shares acquired by the Agent in Open Market Purchases will be allocated to the reinvesting stockholders based on the average cost of such Open Market Purchases. Alternatively, the Agent will allocate Newly Issued Shares to the reinvesting stockholders at a price equal to the average closing price of the respective Fund over the five trading days preceding the payment date of such dividend.

Registered stockholders who acquire their shares through Open Market Purchases and who do not wish to have their Dividends automatically reinvested should so notify the Fund in writing. If a stockholder has not elected to receive cash Dividends and the Agent does not receive notice of an election to receive cash Dividends prior to the record date of any Dividend, the stockholder will automatically receive such Dividends in additional shares.

Participants in the Program may withdraw from the Program by providing written notice to the Agent at least 30 days prior to the applicable Dividend payment date. When a Participant withdraws from the Program, or upon termination of the Program as provided below, certificates for whole shares credited to his/her account under the Program will, upon request, be issued. Whether or not a participant requests that certificates for whole shares by issued, a cash payment will be made for any fraction of a share credited to such account.

The Agent will maintain all stockholder accounts in the Program and furnish written confirmations of all transactions in the accounts, including information needed by stockholders for personal and tax records. The Agent will hold shares in the account of each Program participant in non-certified form in the name of the participant, and each stockholder's proxy will include those shares purchased pursuant to the Program. Each participant, nevertheless, has the right to receive certificates for whole shares owned. The Agent will distribute all proxy solicitation materials to participating stockholders.

In the case of stockholders, such as banks, brokers or nominees, that hold shares for others who are beneficial owners participating in the Program, the Agent will administer the Program on the basis of the number of shares certified from time to time by the record stockholder as representing the total amount of shares registered in the stockholder's name and held for the account

of beneficial owners participating in the Program.

All correspondence concerning the Program should be directed to the Agent at 59 Maiden Lane, New York, New York 10038.

CORPORATE GOVERNANCE PROVISIONS.

Both Funds are Maryland corporations and in many respects have similar charter and by-law provisions.

SPECIAL VOTING PROVISIONS AND REQUIREMENTS.

The Articles of Incorporation and By-laws of each Fund contain provisions that could have the effect of limiting the ability of other entities or persons to acquire control of the Fund, to cause it to engage in certain transactions or to modify its structure. The Board of Directors of each Fund is divided into three classes each having a term of three years. Each year, the term of one class expires and the successor or successors elected to such class will serve for a three-year term. This provision could delay for up to two years the replacement of a majority of the Board of Directors.

The affirmative vote of at least sixty-six and two-thirds (66 2/3%) of the holders of the shares of either of the Funds is required to authorize any of the following transactions:

(i) merger, consolidation or share exchange of either of the Funds with or into any Principal Shareholder (as defined below);
(ii) issuance by either of the Funds of any securities of either of the Funds to any Principal Shareholder for cash;
(iii) sale, lease, or exchange by either of all or any substantial part of the assets of the Funds to any Principal Shareholder (except assets having an aggregate fair market value of less than $1,000,000 aggregating for the purpose of such computation all assets sold, leased or exchanged in any series of similar transactions within a twelve-month period); and
(iv) The sale, lease or exchange to the Funds, in exchange for securities of the Funds, of any assets of any Principal Shareholder (except assets having an aggregate fair market value of less than $1,000,000 aggregating for the purpose of such computation all assets sold, leased or exchanged in any series of similar transactions within a twelve-month period).

Each Fund's By-laws contain provisions the effect of which is to prevent matters, including nominations of directors, from being considered at stockholders' meetings where the Fund has not received sufficient prior notice of the matters.

The Board of Directors of each Fund has determined that the foregoing voting requirements are in the best interests of Stockholders generally. A "Principal Shareholder" is defined in each Fund's respective Articles of Incorporation as any corporation, person or other entity which is the beneficial owner, directly or indirectly, of more than five percent (5%) of the outstanding shares of any class of stock of the respective Fund and shall include any affiliate or associate, as such terms are defined in clause (ii) below, of a Principal Shareholder. In addition to the shares of stock which a corporation, person or other entity beneficially owns directly, (a) any corporation, person

or other entity shall be deemed to be the beneficial owner of any shares of stock of either of the Funds (i) which it has the right to acquire pursuant to any agreement or upon exercise of conversion rights or warrants, or otherwise (but excluding stock option granted by the respective Fund), or (ii) which are beneficially owned, directly or indirectly (including shares deemed owned through application of clause (i) above), by any other corporation, person or entity with which it or its "affiliate" or "associate" (as defined below) has any agreement, arrangement or understanding for the purpose of acquiring, holding, voting or disposing of stock of either Fund, or which is its "affiliate" or "associate," as those terms are defined in Rule 12b-2 of the 1934 Act, and (b) the outstanding shares of any class of stock of either Fund shall include shares deemed owned through application of clauses (i) and (ii) above but shall not include any other shares which may be issuable pursuant to any agreement, or upon exercise of conversions rights or warrants, or otherwise.

BY-LAWS.

Each Fund's By-laws provide, among other things, that:

- certain advance notice requirements must be met in order for Stockholders to submit proposals at annual meetings and for nominations by stockholders for election to the Board of Directors, and
- the power to amend the By-laws is reserved to the Board of Directors, except as otherwise required by the Investment Company Act.

MANAGEMENT OF THE FUNDS

DIRECTORS AND PRINCIPAL OFFICERS.

The business and affairs of each Fund are managed under the direction of that Fund's Board of Directors, and the day-to-day operations are conducted through or under the direction of the officers of that Fund. The Directors and Officers of PGF are also the Directors and Officers of CLM. Please see CLM Proposal 2 for a more thorough discussion of CLM's Directors and Officers.

The following tables set forth the names, ages and principal occupations of each of the Directors of PGF:

Name, Address and Age	Position(s) with Fund	Term of Office Since	Principal Occupation during past 5 years	Directorsh outside of

CLASS I NON-INTERESTED DIRECTORS SERVING UNTIL THE YEAR 2004 ANNUAL MEETING OF

STOCKHOLDERS.

Andrew A. Strauss (48) 77 Central Avenue Suite F Asheville, NC 28801	Director	2000	Attorney and senior member of Strauss & Associates, P.A., Attorneys, Asheville and Hendersonville, N.C.; previous President of White Knight Healthcare, Inc. and LMV Leasing, Inc., a wholly owned subsidiary of Xerox Credit Corporation.	Director o Memorial M and Deerfi Community.
Thomas H. Lenagh (79) 13 Allen's Corner Road Flemington, NJ 08822	Director	2001	Chairman of the Board of Inrad Corp. and Independent Financial Adviser.	Director o Express Co Resources Pharmaceut

CLASS II NON-INTERESTED DIRECTOR SERVING UNTIL THE YEAR 2005 ANNUAL MEETING OF STOCKHOLDERS

Edwin Meese III (70) The Heritage Foundation 214 Massachusetts Ave. NE Washington D.C. 20002	Director	2001	Distinguished Fellow, The Heritage Foundation, Washington D.C.; Distinguished Visiting Fellow at the Hoover Institution, Stanford University; Distinguished Senior Fellow at the Institute of United States Studies, University of London; and Formerly U.S. Attorney General under President Ronald Reagan.	

CLASS III NON-INTERESTED DIRECTORS SERVING UNTIL THE YEAR 2003 ANNUAL MEETING OF STOCKHOLDERS.

Glenn W. Wilcox, Sr. (70) One West Pack Square Suite 1700 Asheville, NC 28801	Director	2000	Chairman of the Board and Chief Executive Officer of Wilcox Travel Agency.	Director o Wachovia C Chairman o University Director, Director, Chairman, real estat

Scott B. Rogers (46) 30 Cumberland Ave. Asheville, NC 28801	Director	2000	Chief Executive Officer, Asheville Buncombe Community Christian Ministry; and President, ABCCM Doctor's Medical Clinic; Appointee, NC Governor's Commission on Welfare to Work.	Director o Chairman a Unlimited Ministeria Southeaste Networkers

INTERESTED DIRECTOR: CLASS II DIRECTOR:

Ralph W. Bradshaw (51)**	Chairman of	1999	President of Cornerstone	Director o

One West Pack Square Suite 1650 Asheville, NC 28801	the Board and President	Advisors, Inc., and of the Funds within the Fund Complex; Financial Consultant; Vice President, Deep Discount Advisors, Inc. (1993-1999).

All of the Directors of PGF served on the Board of Directors for each closed-end fund within the Fund Complex that was managed by Cornerstone Advisors, Inc. ("Cornerstone Advisors"), the Fund's investment manager, during the year ended December 31, 2001. EIS Fund, Inc. was not managed by Cornerstone Advisors until January 2, 2002 and with the exception of Messrs. Lenagh and Meese, all of the members of PGF's Board of Directors, including Mr. Gary A. Bentz, serve on EIS Fund, Inc.'s Board of Directors.

The following table sets forth, for each Director, the aggregate dollar range of equity securities owned of PGF and of all Funds overseen by each Director in the Fund Complex as of June 30, 2002. The information as to beneficial ownership is based on statements furnished to PGF by each Director.

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NON-INTERESTED DIRECTORS:

Name	Dollar Range of Equity Securities in PGF.	Aggregate Dollar Range of Equity Se Funds Overseen by Directors in Fund C
Edwin Meese III	-	-
Andrew A. Strauss	$1-$10,000	$10,001-$50,000
Thomas H. Lenagh	-	-
Glenn W. Wilcox Sr.	$1-$10,000	$10,001-$50,000
Scott B. Rogers	-	-

INTERESTED DIRECTOR:

Name	Dollar Range of Equity Securities in PGF.	Aggregate Dollar Range of Equity Se Funds Overseen by Directors in Fund C
Ralph A. Bradshaw	$10,001-$50,000	$50,001-$100,000

EXECUTIVE OFFICERS

In addition to Mr. Bradshaw, the current officers of PGF are:

Name, Address and Age	Position(s) with Fund	Term of Office Since	Principal Occupation during past 5 years
Gary A. Bentz (46) One West Pack Square Suite 1650 Asheville, NC 28801	Vice President and Treasurer	2001	Chief Financial Officer of Cornerstone Advisors, Inc., Vice President and Treasurer of The Cornerstone Strategic Return Fund, Inc., Cornerstone Strategic Value Fund, Inc. and EIS Fund, Inc.; Financial Consultant; CPA; Chief Financial Officer of Deep Discount Advisors, Inc. (1993-2000).
Thomas R. Westle (48) 405 Park Avenue New York, NY 10022	Secretary	2001	Partner of Spitzer & Feldman P.C., a law firm, and previous Partner at Battle Fowler LLP; Secretary of The Cornerstone Strategic Return Fund, Inc., Cornerstone Strategic Value Fund, Inc. and EIS Fund, Inc.

PGF pays each of its Directors who is not a director, officer, partner, co-partner or employee of Cornerstone Advisors or any affiliate thereof a stipend of $6,000, a fee in the amount of $600 per Board Meeting, and a fee of $100 per Special Telephonic Board Meeting. PGF has an Audit and Nominating Committee each of which is comprised of all of the Non-interested members of the Board of Directors. Committee members that attend the Committee Meetings shall receive a fee of $200 per meeting attended. In addition, PGF will reimburse those Directors for travel and out-of-pocket expenses incurred in connection with Board of Directors meetings. The aggregate remuneration paid to Directors by PGF during the fiscal year ended December 31, 2001 was $68,816, and the aggregate remuneration paid to Directors by CLM during the fiscal year ended December 31, 2001 was $77,500.

Name of Director	Aggregate Compensation From PGF	Total Compensation From Fund and Fund Complex* Paid to Director
Ralph W. Bradshaw	$24,671	$58,621
Glenn W. Wilcox, Sr.	$7,850	$26,150
Andrew A. Strauss	$7,850	$26,150
Edwin Meese III	$6,650	$22,450
Scott B. Rogers	$7,850	$26,150
Thomas H. Lenagh	$6,650	$23,000

William A. Clark**	$7,295	$31,745

The Articles of Incorporation and By-laws of each Fund provide that the Funds will indemnify directors and officers and may indemnify employees or agents of the Funds against liabilities and expenses incurred in connection with litigation in which they may be involved because of their positions with the Funds to the fullest extent permitted by law. In addition, each Fund's Articles of Incorporation provide that the Funds' directors and officers will not be liable to Stockholders for money damages, except in limited instances.

INVESTMENT ADVISER.

Cornerstone Advisors is the investment adviser to both PGF and CLM pursuant to investment advisory agreements with each.

Cornerstone Advisors, which has its principal office at One West Pack Square, Suite 1650, Asheville, North Carolina 28801, was incorporated in February of 2001 and began operations in April of 2001, to provide investment management services to closed-end investment companies and is registered with the Securities and Exchange Commission under the Investment Company Act. In addition to providing investment management services to PGF and CLM, Cornerstone Advisors also provides investment management services to two other closed-end funds, The Cornerstone Strategic Return Fund, Inc. and EIS Fund, Inc. (f/k/a Excelsior Income Shares, Inc.). Mr. Ralph W. Bradshaw, a Director and President of PGF and CLM, serves as each Fund's portfolio manager. The annual advisory fee payable by the Fund under the Cornerstone Agreement is equal to one (1%) percent of the Fund's average weekly net assets.

Messrs. Ralph Bradshaw and Gary Bentz are the sole stockholders of Cornerstone Advisors and each have had extensive experience with closed-end investment companies. Mr. Bradshaw, served as a Vice President of Deep Discount Advisors, Inc. ("Deep Discount"), a large stockholder of both PGF and CLM, from 1993 to 1999, and Mr. Bentz was affiliated with Deep Discount as its Chief Financial Officer from 1993 to 2000. Messrs. Bradshaw and Bentz no longer possess any ownership interest in Deep

Discount nor do they provide any services to Deep Discount or its clients. There exists no arrangements or understandings among Cornerstone Advisors, Deep Discount, ROIMC or any of their respective stockholders with respect to the Funds.

Deep Discount and Ron Olin Investment Management Company ("ROIMC"), both of which jointly filed a Schedule 13G with the Securities and Exchange Commission (the "SEC") on February 15, 2002, as beneficial owners of more than five (5%) percent of the outstanding shares of each Fund, are registered investment advisers which, on behalf of their respective advisory clients, invest in the common stock of closed-end investment companies.

Cornerstone Advisors has sole investment discretion for each Fund's assets under the supervision of each Fund's Board of Directors and in accordance with each Fund's stated policies. Cornerstone Advisors selects investments for each Fund and places purchase and sale orders on behalf of the Funds.

ADMINISTRATOR.

Bear Stearns Funds Management Inc. ("BSFM") serves as each Fund's administrator pursuant to an administrative agreement with each Fund. BSFM is located at 383 Madison Avenue, 23rd Floor, New York, New York 10179.

BSFM provides office facilities and personnel adequate to perform the following services for each Fund:

- oversight of the determination and publication of each Fund's net asset value in accordance with the respective Fund's policy as adopted from time to time by the respective Board of Directors,
- maintenance of the books and records of each Fund as required under the Investment Company Act,
- preparation of each Fund's U.S. federal, state and local income tax returns,
- preparation of financial information for each Fund's proxy statements and semi-annual and annual reports to Stockholders, and
- preparation of certain of each Fund's reports to the SEC.

As of June 30, 2002, BSFM provided accounting and/or administrative services for 29 investment companies and investment partnerships, with combined total assets of approximately $6.6 billion.

CUSTODIAN.

Custodial Trust Company, 101 Carnegie Center, Princeton, New Jersey, is the custodian for both Funds' assets.

TRANSFER AGENT AND REGISTRAR.

American Stock Transfer & Trust Co., 59 Maiden Lane, New York, New York 10038 acts as the transfer agent and registrar of each Fund.

ESTIMATED EXPENSES.

Except as otherwise provided in the administrative services agreements, Cornerstone Advisors and BSFM are each obligated to pay expenses associated with providing the services contemplated by the agreements to which they are parties, including compensation of and office space for their respective officers and employees connected with investment and economic research, trading and investment management and administration of each Fund, as well as the fees of all directors of each Fund who are affiliated with those companies or any of their affiliates. Each Fund pays all other expenses incurred in the operation of that Fund including, among other things:

- expenses for legal and independent accountants' services,
- costs of printing proxies, stock certificates and stockholder reports,
- charges of the custodians, and the transfer and dividend- paying agent's expenses in connection with the Funds' Dividend Reinvestment and Cash Purchase Plan,
- fees and expenses of unaffiliated directors,
- accounting and pricing costs,
- membership fees in trade associations,
- fidelity bond coverage for the Funds' officers and employees,

- directors' and officers' errors and omissions insurance coverage,
- brokerage costs and stock exchange fees,
- taxes,
- stock exchange listing fees and expenses, and
- other extraordinary or non-recurring expenses and other expenses properly payable by the Funds.

CONTROL PERSONS AND PRINCIPAL HOLDERS OF SECURITIES.

The following table shows certain information based on filings made with the SEC concerning persons who may be deemed beneficial owners of 5% or more of the shares of common stock of either Fund because they possessed or shared voting or investment power with respect to the shares of that Fund:

	PGF(1)		
	SHARES OF COMMON STOCK BENEFICIALLY OWNED		SHARES OF C
NAME AND ADDRESS OF BENEFICIAL OWNER	AMOUNT	%	AM
Deep Discount Advisors, Inc. (2) One West Pack Square Suite 777 Asheville, NC 28801	721,900	16.8%	73
Ron Olin Investment Management Company (2) One West Pack Square Suite 777 Asheville, NC 28801	1,812,600	42.2%	70
Ronald G. Olin (3) One West Pack Square Suite 777 Asheville, NC 28801	356,707	33.1%	N
Karpus Management, Inc. (4) D/b/a Karpus Investment Management 183 Sullys Trail Pittsford, NY 14534	N/A	N/A	54

All the directors and executive officers, as a group, of PGF, as of June 30, 2002, owned less than 1% of the outstanding shares of PGF, and all the directors and executive officers, as a group, of CLM, as of the same date, owned less than 1% of the outstanding shares of CLM.

EXPERTS

Each Fund previously used PricewaterhouseCoopers LLP, Two Commerce Square, Philadelphia, PA 19103, as its independent public accountants who audited each Funds financial statements for the fiscal year ended December 31,

2001. On April 19, 2002, PGF's stockholders ratified the selection of Tait, Weller & Baker as the Fund's independent accountants for the year ending December 31, 2002.

Currently, CLM, in the event that the Merger is not consummated, is requesting that the Fund's stockholders contingently ratify the decision, by the Fund's Board of Directors, to engage Tait, Weller & Baker as independent public accountants. See CLM Proposal 3.

REQUIRED VOTE

The Merger has been approved by the Board of Directors of each Fund. Approval of the Merger requires the affirmative vote of the holders of a majority of the outstanding shares of common stock of each Fund. Therefore an abstention is equivalent to a vote against the Merger. The Board of Directors of each Fund recommends that the Stockholders vote in favor of this Proposal 1.

LEGAL PROCEEDINGS

There are currently no material legal proceedings to which the Funds are a party.

LEGAL OPINIONS

Certain legal matters in connection with the Merger will be passed upon for the Funds by Spitzer & Feldman P.C.

II. ADDITIONAL PROPOSAL TO BE VOTED ON BY PGF STOCKHOLDERS WHICH WILL ONLY TAKE EFFECT IN THE EVENT THAT PROPOSAL 1 IS APPROVED BY BOTH FUNDS STOCKHOLDERS.

PGF PROPOSAL 2

RATIFICATION OF THE CHANGE IN THE NAME OF THE FUND FROM "PROGRESSIVE RETURN FUND, INC." TO "PROGRESSIVE TOTAL RETURN FUND, INC."

In connection with the proposed merger of PGF and CLM, the Board of Directors of PGF authorized an amendment to PGF's Articles of Incorporation to change the name of the Fund from "Progressive Return Fund, Inc." to "Progressive Total Return Fund, Inc." which will only take effect in the event that the proposed merger is approved by the shareholders of both Funds. Under the Maryland General Corporation Law, an amendment to a Charter, which changes the name of the corporation, must be authorized by the Board of Directors and ratified by a majority of the outstanding shares entitled to vote.

At the Board of Directors Meeting held on August 2, 2002, the Board of Directors unanimously authorized the amendment to the Articles of Incorporation to change the name of the Fund from "Progressive Return Fund,

Inc." to "Progressive Total Return Fund, Inc.", as set forth on Exhibit B.

Accordingly, the Board of Directors believes that, subject to shareholder ratification of PGF Proposal 2, changing the name of the Fund to "Progressive Total Return Fund, Inc." is necessary and appropriate and in the best interests of the Fund and its shareholders.

REQUIRED VOTE

Ratification of the name change requires the affirmative vote of the holders of a majority of PGF's outstanding voting securities. If the name change is approved by the PGF's shareholders and the Merger is consummated, such change will become effective immediately following the filing of the Fund's Certificate of Amendment to the Articles of Incorporation with the Maryland Secretary of State.

THE BOARD OF DIRECTORS, INCLUDING THE NON-INTERESTED DIRECTORS, RECOMMENDS THAT THE SHAREHOLDERS VOTE "FOR" THE RATIFICATION OF THE AMENDMENT TO THE FUND'S ARTICLES OF INCORPORATION TO CHANGE THE NAME OF THE FUND FROM "PROGRESSIVE RETURN FUND, INC." TO "PROGRESSIVE TOTAL RETURN FUND, INC."

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III. ADDITIONAL PROPOSALS TO BE VOTED ON BY CLM'S STOCKHOLDERS WHICH WILL ONLY TAKE EFFECT IN THE EVENT THAT THE MERGER IS NOT CONSUMMATED.

CLM PROPOSAL 2:

ELECTION OF DIRECTORS

In accordance with the Fund's By-Laws, the Fund's Board of Directors is divided into three classes: Class I, Class II and Class III. Each class has a term of three years and each year the term of office of one class expires. The effect of these staggered terms is to limit the ability of other entities or persons to acquire control of the Fund by delaying the replacement of a majority of the Board of Directors.

At the Meeting, stockholders will be asked to elect two Class I Directors to hold office until the year 2005 Annual Meeting of Stockholders or thereafter until each of their respective successors is duly elected and qualified. The term of office of the Class II Directors, currently consisting of Messrs. Thomas H. Lenagh and Scott B. Rogers, expires at the year 2003 Annual Meeting of Stockholders or thereafter in each case until their successors are duly elected and qualified. The term of office of the Class III Directors, Messrs. Glenn W. Wilcox, Sr. and Andrew A. Strauss, expires at the year 2004 Annual Meeting of Stockholders or thereafter in each case until their successors are duly elected and qualified.

At the Meeting, stockholders will be asked to vote for the election of Messrs. Ralph W. Bradshaw and Edwin Meese III as Class I Directors to serve until the year 2005 Annual Meeting of Stockholders or thereafter until each of their successors is duly elected and qualified. If elected, each nominee has consented to serve as a director of the Fund until his successor is duly elected and qualified.

The persons named in the accompanying form of proxy intend to vote at the Meeting (unless directed not to vote) FOR the election of Messrs. Ralph W.

Bradshaw and Edwin Meese III. Each nominee has indicated that he will serve if elected, and the Board of Directors has no reason to believe that any of the nominees named above will become unavailable for election as a director, but if any nominee should be unable to serve, the proxy will be voted for any other person determined by the persons named in the proxy in accordance with their judgment.

The following table sets forth the names, addresses, ages and principal occupations of each of the nominees for election as Class I Directors:

NOMINEES

Name, Address and Age	Position with Fund	Term of Office Since	Principal Occupation during past 5 years	Di No of
CLASS I NON-INTERESTED NOMINEE TO SERVE UNTIL THE YEAR 2005 ANNUAL MEETING OF STOCKHOLDERS:				
Edwin Meese III (70) The Heritage Foundation 214 Massachusetts Ave. NE Washington D.C. 20002	Director	2001	Distinguished Fellow, The Heritage Foundation, Washington D.C.; Distinguished Visiting Fellow at the Hoover Institution, Stanford University; Distinguished Senior Fellow at the Institute of United States Studies, University of London; and Formerly U.S. Attorney General under President Ronald Reagan.	
INTERESTED NOMINEE TO SERVE UNTIL THE YEAR 2005 ANNUAL MEETING OF STOCKHOLDERS:				
Ralph W. Bradshaw (51)** One West Pack Square Suite 1650 Asheville, NC 28801	Chairman of the Board and President	1998	President of Cornerstone Advisors, Inc., and of the Funds within the Fund Complex; Financial Consultant; Vice President, Deep Discount Advisors, Inc. (1993-1999).	Di

REMAINING BOARD OF DIRECTORS

The following tables set forth the names, addresses, ages and principal occupations of each of the remaining Directors of the Fund:

Name, Address and Age	Position(s) with Fund	Term of Office Since	Principal Occupation during past 5 years	Directors Outside o
CLASS II NON-INTERESTED DIRECTORS SERVING UNTIL THE YEAR 2003 ANNUAL MEETING OF STOCKHOLDERS:				
Scott B. Rogers (46) 30 Cumberland Ave. Asheville, NC 28801	Director	2000	Chief Executive Officer, Asheville Buncombe Community Christian Ministry; and President, ABCCM Doctor's Medical Clinic; Appointee, NC Governor's Commission on Welfare to Work.	Director Chairman Unlimited Ministeri Southeast Networker
Thomas H. Lenagh (79) 13 Allen's Corner Road Flemington, NJ 08822	Director	1987	Chairman of the Board of Inrad Corp. and Independent Financial Adviser.	Director Express C Resources Pharmaceu
CLASS III NON-INTERESTED DIRECTORS SERVING UNTIL THE YEAR 2003 ANNUAL MEETING OF STOCKHOLDERS:				
Glenn W. Wilcox, Sr. (70) One West Pack Square Suite 1700 Asheville, NC 28801	Director	2000	Chairman of the Board and Chief Executive Officer of Wilcox Travel Agency.	Director Inc.; Wac and Chair Universit Director, Director, Inc.; and Associate venture)
CLASS III NON-INTERESTED DIRECTORS CONTINUED:				
Andrew A. Strauss (48) 77 Central Avenue Suite F Asheville, NC 28801	Director	2000	Attorney and senior member of Strauss & Associates, P.A., Attorneys, Asheville and Hendersonville, NC; previous President of White Knight Healthcare, Inc. and LMV Leasing, Inc., a wholly owned subsidiary of Xerox Credit Corporation.	Director Inc.; Mem Foundatio Retiremen

The following table sets forth, for each Director, the aggregate dollar range of equity securities owned of the Fund and of all Funds overseen by each Director in the Fund Complex as of December 31, 2001. The information as to beneficial ownership is based on statements furnished to the Fund by each

Director.

NON-INTERESTED DIRECTORS:

Name	Dollar Range of Equity Securities in CLM.	Aggregate Dollar Range Securities in All Funds Directors in Fund Compl
Edwin Meese III	-	-
Andrew A. Strauss	$1-$10,000	$10,001-$50,000
Thomas H. Lenagh	-	-
Glenn W. Wilcox Sr.	$1-$10,000	$10,001-$50,000
Scott B. Rogers	-	-

INTERESTED DIRECTOR:

Name	Dollar Range of Equity Securities in CLM.	Aggregate Dollar Rang Securities in All Fun Directors in Fund Com
Ralph W. Bradshaw	$10,001-$50,000	$50,001-$100,000

EXECUTIVE OFFICERS

In addition to Mr. Bradshaw, the current officers of CLM are:

Name, Address and Age	Position(s) with Fund	Term of Office Since	Principal Occupation during past 5 years	Di
Gary A. Bentz (46) One West Pack Square Suite 1650 Asheville, NC 28801	Vice President and Treasurer	2001	Chief Financial Officer of Cornerstone Advisors, Inc., Vice President and Treasurer of Progressive Return Fund, Inc., The Cornerstone Strategic Return Fund, Inc. and EIS Fund, Inc.; Financial Consultant; CPA; Chief Financial Officer of Deep Discount Advisors, Inc. (1993-2000).	Di
Thomas R. Westle (48) 405 Park Avenue New York, NY 10022	Secretary	2001	Partner of Spitzer & Feldman P.C., a law firm, and previous Partner at Battle Fowler LLP; Secretary of Progressive Return Fund, Inc., The Cornerstone Strategic Return Fund, Inc. and EIS Fund, Inc.	

Under the federal securities laws, the Fund is required to provide to stockholders in connection with the Meeting, information regarding compensation paid to Directors by the Fund as well as by the various other U.S. registered investment companies advised by

the Fund's investment manager during its prior fiscal year. The following table provides information concerning the compensation paid during the year ended December 31, 2001, to each Director of the Fund. All of the Directors received compensation for serving as a Director of The Cornerstone Strategic Return Fund, Inc. and Progressive Return Fund, Inc., which were also managed by Cornerstone Advisors during the year ended December 31, 2001. Please note that the Fund has no bonus, profit sharing, pension or retirement plans.

Name of Director	Director Since	Aggregate Compensation From CLM	Total Compensation From Fun Fund Complex* Paid to Dire
Ralph W. Bradshaw	1998	$17,500	$58,621
Glenn W. Wilcox, Sr.	2000	$10,000	$26,150
Andrew A. Strauss	2000	$10,000	$26,150
Edwin Meese III	2001	$7,500	$22,450
Scott B. Rogers	2000	$10,000	$26,150
Thomas H. Lenagh	1987	$10,000	$23,000
William A. Clark**	1999	$12,500	$31,745

Each Director attended at least seventy-five (75%) percent or more of the six (6) meetings of the Board of Directors (including regularly scheduled and special meetings) held during the period for which he was a Director.

The Fund has a nominating committee which is comprised of the all of the Non-interested directors.

AUDIT COMMITTEE

The Fund's Audit Committee is currently composed of five Non-Interested directors, Messrs. Wilcox, Strauss, Meese, Lenagh and Rogers. The principal functions of the Audit Committee include but are not limited to: (i) recommendations to the Board for the appointment of the Fund's independent accountants; (ii) review of the scope and anticipated cost of the independent accountant's audit; and (iii) consideration of the independent accountant's reports concerning their conduct of the audit, including any comments or recommendations the Board of Directors might make in connection thereto. The Audit Committee convened three times during the fiscal year ended December 31, 2001. Each member of the Audit Committee attended at least seventy-five percent (75%) or more of the three meetings of the Audit Committee.

On June 1, 2000, the Audit Committee, followed by the full Board of Directors, adopted a written charter setting forth the duties and responsibilities of the Audit Committee, and such charter was reapproved by the Board of Directors on February 9, 2001 and February 14, 2002, respectively. The Audit Committee recommends to the Board of Directors, subject to stockholder

approval, the selection of Tait, Weller & Baker, as the Fund's independent accountants.

On February 25, 2002, the Board of Directors and the Audit Committee determined to replace PricewaterhouseCoopers LLP ("PwC") as the Fund's independent accountants. PwC's accountant report for the past two years did not contain any adverse opinion or any qualification as to uncertainty, audit scope or accounting principles. Further, the Board's decision to replace PwC was not due to any disagreement on any matter of accounting principles or practices, financial statement disclosure or auditing scope or procedure.

The following table sets forth the aggregate fees billed by PricewaterhouseCoopers LLP, the independent accountants for the Fund's most recent fiscal year, for professional services rendered for: (i) the audit of the Fund's annual financial statements and the review of financial statements included in the Fund's reports to stockholders ("Audit Fees"); (ii) financial information systems design and implementation services provided to the Fund, its investment manager and entities that control, are controlled by or under common control with the Fund's investment manager that provides services to the Fund ("Financial Information Systems Design"); and (iii) all other services provided to the Fund, its investment manager and entities that control, are controlled by or under common control with the Fund's investment manager that provides services to the Fund ("All Other Fees").

AUDIT FEES	FINANCIAL INFORMATION SYSTEMS DESIGN	ALL OTHER FEES
$29,750	$-	$3,000

The Fund has no compensation committee.

AUDIT COMMITTEE REPORT

The Audit Committee has met and held discussions with the Fund's Administrator, Bear Stearns Funds Management Inc., and the Fund's independent accountants. The independent accountants represented to the Audit Committee that the Fund's financial statements were prepared in accordance with U.S. generally accepted accounting principles, and the Audit Committee has reviewed and discussed the financial statements with the Fund's Administrator and its independent accountants. The Audit Committee also discussed with the independent accountants matters required to be discussed by Statement on Auditing Standards No. 61.

The Fund's independent accountants also provided to the Audit Committee the written disclosures required by Independence Standards Board Standard No. 1 (Independence Discussions with Audit Committees), and the Audit Committee discussed with the independent accountants' their independence, in light of the services they were providing.

Based upon the Audit Committee's discussion with the Fund's Administrator and the independent accountants and the Audit Committee's review of the representations of the independent accountants to the Audit Committee, the Audit Committee recommended that the Board of Directors include the audited

financial statements in the Fund's Annual Report for the fiscal year ended December 31, 2001 filed with the Securities and Exchange Commission.

Respectfully submitted,

Edwin Meese III
Glenn W. Wilcox, Sr.
Andrew A. Strauss
Thomas H. Lenagh
Scott B. Rogers

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SECTION 16(A) BENEFICIAL OWNERSHIP REPORTING COMPLIANCE

Section 16(a) of the Securities Exchange Act of 1934 (the "Exchange Act") and Section 30(h) of the 1940 Act in combination require the Fund's directors and officers, persons who own more than ten (10%) of the Fund's common stock, and the Fund's investment manager and its directors and officers, to file reports of ownership and changes in ownership with the Securities and Exchange Commission and the New York Stock Exchange, Inc. The Fund believes that the Fund's directors and officers, the Fund's investment manager and its directors and officers have complied with all applicable filing requirements during the year ended December 31, 2001.

REQUIRED VOTE

Directors are elected by a plurality (a simple majority of the votes cast at the meeting) of the votes cast by the holders of shares of common stock of the Fund present in person or represented by proxy at a meeting with a quorum present. For purposes of the election of Directors, abstentions and broker non-votes will be counted as shares present for quorum purposes, will be considered votes cast, and will affect the plurality vote required for Directors.

THE BOARD OF DIRECTORS RECOMMENDS THAT THE STOCKHOLDERS VOTE "FOR" THE ELECTION OF MESSRS. EDWIN MEESE III AND RALPH W. BRADSHAW AS CLASS I DIRECTORS OF CLM.

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CLM PROPOSAL 3:

RATIFICATION OF SELECTION OF INDEPENDENT ACCOUNTANTS

The second proposal to be submitted will be the ratification or rejection of the selection by the Board of Directors of Tait, Weller & Baker as independent accountants of the Fund for the year ending December 31, 2002. At a meeting held on February 25, 2002, the Board of Directors, including those directors who are not "interested persons" of the Fund, approved the selection of Tait, Weller & Baker for the year ending December 31, 2002 and determined to replace PricewaterhouseCoopers LLP. Such selection is being submitted to the stockholders for ratification. The engagement of Tait, Weller & Baker is conditioned on the right of the Fund, by majority vote of its stockholders, to

terminate such employment.

Tait, Weller & Baker has informed the Fund that it has no material direct or indirect financial interest in the Fund. A representative of Tait, Weller & Baker will be available by telephone at the Meeting and will have the opportunity to make a statement if the representative so desires and will be available to respond to appropriate questions.

REQUIRED VOTE

Ratification of the selection of Tait, Weller & Baker as independent accountants of the Fund requires the affirmative vote of the holders of a simple majority, defined as a majority of the votes cast by holders of shares of common stock of the Fund present in person or represented by proxy at a meeting with a quorum present. For purposes of this proposal, abstentions and broker non-votes will be counted as shares present at the Meeting for quorum purposes and will have no effect on the outcome of this proposal.

THE BOARD OF DIRECTORS, INCLUDING THE "NON-INTERESTED" DIRECTORS, RECOMMENDS THAT THE STOCKHOLDERS VOTE "FOR" THE RATIFICATION OF TAIT, WELLER & BAKER AS CLM'S INDEPENDENT ACCOUNTANTS.

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CLM PROPOSAL 4:

SHAREHOLDER PROPOSAL REQUESTING THAT THE FUND
BE CONVERTED INTO AN OPEN-END FUND

Karpus Management, Inc. d/b/a Karpus Investment Management ("KIM"), 183 Sully's Trail, Pittsford, New York, New York 14534, has submitted the following proposal for inclusion in this Proxy Statement. KIM stated that it has owned shares of the Fund with a market value of at least $2,000 continuously for the preceding year and intends to maintain the required ownership through the date of the Meeting. The Board of Directors and the Fund accept no responsibility for the accuracy of either the proposal or of KIM's supporting statement.

STOCKHOLDER PROPOSAL

Karpus Investment Management proposes: Cornerstone Strategic Value Fund, Inc. (CLM) be converted to an open-end fund within 90 days after acceptance by the shareholders.

SUPPORTING STATEMENT

It is the belief of KIM that current Fund Management of CLM is not making significant strides in closing the discount at which the Fund trades. For the time period from January 5, 2001 through December 7, 2001 the Fund has traded at an average discount of 15.79%.

Management claims that the share buy back program can help close this discount over time. It is the opinion of KIM this cannot happen simply by the Fund repurchasing shares. KIM believes that drastic steps must occur for the shareholders to recognize the full economic value of their investment.

KIM believes the only way for shareholders to reap the full value of their investment is to open-end the Fund. If this would occur, shareholders would immediately increase the value of their investment by 14.46% (based on the net asset value of December 7, 2001)!

It is the opinion of KIM that the current Fund Management may not have sufficient experience to be the best choice for managing the Fund. KIM believes that the Fund's Manager lacks adequate experience in managing individual securities (only funds in a closed-end format). The current manager does not have a track record, known to KIM, to instill our confidence in their abilities.

Poor performance in both price and net asset value does not have to be tolerated by the shareholders. Management will claim that they are doing a good job and they have not been the manager long enough for shareholders to recognize their abilities.

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KIM believes that the shareholders must act now. Time is not on the side of the shareholders to wait!

From January 4, 2001 through December 6, 2001 the net asset value performance of CLM has equaled - 19.4518% (-20.9417 annual equivalent). The price performance of the Fund has been equally dismal. For the same holding period price performance equaled -20.80% (-22.3781 annual equivalent)(All calculations by Bloomberg). KIM believes that the shareholders deserve better performance than what has been delivered in 2001.

CLM is plagued by low trading volume. Trading volume from January 4, 2001 through December 6, 2001 has averaged a mere 8,706 shares. It is KIM's opinion that shareholders who wish to liquidate large positions could severely depress the price at which the Fund trades. This could cause economic harm to shareholders remaining in CLM.

KIM believes open ending is the only possible method for shareholders to recognize the economic reality of their investment. Open ending would allow shareholders, such as KIM, who do not have confidence in the direction of the Fund's management, to get out of the Fund.

Should CLM be open ended at net asset value, shareholders would recognize an immediate economic benefit of approximately 14.46% (based on price of $7.93 and NAV of $9.27 as of 12/7/01).

KIM further believes that any Investment Adviser is not fulfilling their Fiduciary duty to their clients if they do not vote to open end CLM.

STATEMENT OF POSITION OF THE BOARD OF DIRECTORS IN OPPOSITION TO THE SHAREHOLDER PROPOSAL

The shareholder proposal asks that the Fund be converted to an open-end fund in order to provide full Net Asset Value (NAV) to those shareholders wishing to leave the Fund. All of the Directors believe that this is not the most effective means to deliver long-term added value to a majority of shareholders. The full Board opposes the proposal and believes that

open-ending should be rejected in favor of other means of maximizing shareholder value within the closed-end structure. The Board believes that somewhat more patience is justified in an attempt to reap potentially greater rewards. The goal of this Board is not to pit one shareholder against another, but to establish a balance that satisfies the greatest number of shareholders.

During the first quarter of 2001, the Fund substantially under-performed the S&P 500 benchmark, which fell 12.1%. Following Cornerstone Advisors' becoming the Fund's investment manager, after the end of the first quarter of 2001, the benchmark continued to decline through the end of the year as the U.S. entered a recession in March which was followed by the September 11th tragedy and its aftermath.

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In spite of this challenging environment over the last three quarters of 2001, the Fund's price appreciated 3.9% and the Fund's discount to NAV closed to 12.5% by the end of the year. While nine months is not enough time for effective evaluation, we believe our approach that includes repurchasing shares at a discount, optimizing Fund expenses, and diversifying the Fund's portfolio has and will continue to create significant added value for our shareholders.

Different types of investors have their own agendas and their own beliefs. The closed-end structure is fundamentally different from an open-end structure or one that provides NAV on demand. Attempts to deliver NAV immediately to a minority of shareholders who wish to exit the Fund may well destroy or diminish the advantages otherwise enjoyed by the other shareholders. For the time being, the current Board is committed to realizing the potential of the Fund without changing its fundamental nature.

The major benefits of the closed-end structure to long-term shareholders are threefold: flexibility in managing fund assets, lower expenses, and performance enhancement through profiting from the discount.

Flexibility in managing fund assets. Unlike open-end funds, closed-end funds are not subject to cash flow disruptions caused by inflows or outflows of capital when shareholders buy new shares or redeem shares. This permits Fund management to take a more long-term perspective on investments and may permit a more effective investment strategy. This may in turn produce higher long-term portfolio returns. In addition, cash can be raised to take advantage of anticipated market declines without fear that it will instead have to be used to satisfy the shareholder redemptions in open-end funds that normally accompany market reversals. Less liquid securities, such as other closed-end funds selling at discounts, can be placed in the Fund's portfolio without fear that redemptions will require untimely sales to raise capital.

Lower expenses. Because closed-end funds need not engage in many of the shareholders services normally required of open-end funds and do not have the same marketing and communication activities, costs can be kept to a minimum. The current Directors have found many ways to reduce expenses and are pursuing many more. The Board remains convinced that closed-end funds can be run more cost effectively than open-end funds and that these savings, along with the additional flexibility in managing Fund assets, may well permit substantial additional returns to be realized over time as compared with equivalent open-end funds.

Profiting from the discount. Closed-end funds often sell at discounts, at least part of the time. A fund that purchases its own shares at a discount benefits loyal, long-term shareholders in two ways. First, the net

asset value is automatically increased at no additional risk. Second, the supply of shares available for sale at a discount is reduced and this creates price pressure which is likely to reduce the discount and enhance share value. While the extra liquidity may benefit shareholders who choose to sell their shares, the greatest value of an ongoing buyback program accrues to long-term shareholders.

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Shareholders who view the fund as a long-term, tax efficient investment may be better off in a closed-end structure at a nominal or moderate discount which fluctuates.

For all these reasons, the Board unanimously recommends that stockholders vote AGAINST this stockholder proposal.

EFFECT OF PASSAGE OF THE PROPOSAL

CLM Proposal No. 4 requires the affirmative vote of a majority of shares voting at the Meeting for passage. The Investment Company Act of 1940 requires that any conversion of a closed-end investment company to an open-end investment company be by a vote of a majority of the Fund's outstanding voting securities. The term "a majority of the Fund's outstanding voting securities" is defined by the 1940 Act to mean the vote, at the annual or a special meeting of the security holders of such company duly called (a) of 67 per centum or more of the voting securities present at such meeting, if the holders of more than 50 per centum of the outstanding voting securities of such company are present or represented by proxy; or (b) of more than 50 per centum of the outstanding voting securities of such company, whichever is the less.

THE BOARD OF DIRECTORS UNANIMOUSLY RECOMMENDS THAT STOCKHOLDERS VOTE AGAINST PROPOSAL NO. 4

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ADDITIONAL INFORMATION

The Proxy Statement/Prospectus does not contain all of the information set forth in the registration statements and the exhibits relating thereto which the Funds have filed with the Commission, under the Securities Act and the Investment Company Act, to which reference is hereby made.

The Funds are subject to the informational requirements of the Exchange Act and in accordance therewith, file reports and other information with the SEC. Reports, proxy statements, registration statements and other information filed by the Funds can be inspected and copied at the public reference facilities of the SEC in Washington, D.C. Copies of such materials also can be obtained by mail from the Public Reference Branch, Office of Consumer Affairs and Information Services, Securities and Exchange Commission, Washington, D.C. 20594, at prescribed rates.

OTHER MATTERS TO COME BEFORE THE MEETING.

The Board of Directors of each Fund is not aware of any matters that will be presented for action at the Meeting other than the matters set forth herein. Should any other matters requiring a vote of Stockholders arise, the proxy in the accompanying form will confer upon the person or persons entitled to vote the shares represented by such proxy the discretionary authority to vote the shares as to any such other matters in their discretion in the interest of the respective Fund. PLEASE COMPLETE, SIGN AND RETURN THE ENCLOSED PROXY CARD(S) PROMPTLY. NO POSTAGE IS REQUIRED IF MAILED IN THE UNITED STATES.

By order of the Boards of Directors of Progressive Return Fund, Inc. and Cornerstone Strategic Value Fund, Inc.

PROGRESSIVE RETURN FUND, INC.

Ralph W. Bradshaw, President

CORNERSTONE STRATEGIC VALUE FUND, INC.

Ralph W. Bradshaw, President

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PROGRESSIVE RETURN FUND, INC.
CORNERSTONE STRATEGIC VALUE FUND, INC.
SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

	CORNERSTONE STRATEGIC VALUE FUND, INC.		PROGRESSIVE R FUND, INC.	
Description	Principal Amount (000's)	Value	Principal Amount (000's)	Value
EQUITY SECURITIES - 96.06%				
CLOSED-END DOMESTIC FUND - 2.03%				
Gabelli Global Multimedia Trust, Inc.	16,000	$ 112,000		
John Hancock Bank & Thrift Opportunity Fund	32,500	276,575	92,600	$ 788,026
		388,575		
CONSUMER DISCRETIONARY - 12.82%				
AOL Time Warner Inc.*	2,500	36,775	14,250	209,618
Bed, Bath & Beyond Inc.			1,300	49,062
Best Buy Co., Inc.			1,250	45,375

Carnival Corp.	2,100	58,149	2,700	74,763
Circuit City Stores-Circuit City Group			1,000	18,750
Clear Channel Communications, Inc.*	2,100	67,242	2,700	86,454
Comcast Corp., Special Class A			4,100	96,063
Delphi Corp.	2,000	26,400	2,600	34,320
Dollar General Corp.			1,500	28,545
Eastman Kodak Co.			1,400	40,838
Federated Department Stores, Inc.			1,000	39,700
Ford Motor Co.	6,500	104,000	5,800	92,800
Gannett Co., Inc.	2,000	151,800	1,200	91,080
General Motors Corp.	1,900	101,555	2,600	138,970
Harley Davidson, Inc.			1,400	71,778
Hilton Hotels Corp.			1,700	23,630
Home Depot, Inc. (The)	41,100	1,509,603	7,500	275,475
J.C. Penney Co., Inc.			1,300	28,626
Johnson Controls, Inc.			1,000	81,610
Limited Brands			2,500	53,250
Lowe's Companies, Inc.			2,600	118,040
Marriott International, Inc., Class A			1,100	41,855
Mattel, Inc.			2,500	52,525
May Department Stores Co. (The)			1,400	46,102
McDonald's Corp.	4,600	130,870	4,000	113,800
Newell Rubbermaid Inc.			1,300	45,578
NIKE, Inc., Class B			1,300	69,745
Office Depot, Inc.*			1,400	23,520
Omnicom Group Inc.	1,000	45,800	1,600	73,280
Sears, Roebuck & Co.			1,600	86,880
Staples, Inc.*			2,500	49,250
Starbucks Corp.*			1,700	42,245
Target Corp.	3,200	118,848	4,100	152,274
TJX Companies, Inc.			2,600	50,986
Toys "R" Us, Inc.*			1,000	17,470
Tribune Co.			1,400	60,900
Viacom Inc., non-voting Class B*	6,000	266,220	6,900	306,153
Wal-Mart Stores, Inc.	15,800	869,158	13,500	742,635
Walt Disney Co. (The)	7,200	136,080	6,500	122,850
		3,622,500		3,796,795
CONSUMER STAPLES - 11.24%				
Anheuser-Busch Companies, Inc.	3,200	160,000	1,600	80,000
Archer-Daniels-Midland Co.	2,415	30,888	3,045	38,946
Avon Products, Inc.			1,200	62,688
Campbell Soup Co.			2,000	55,320
Clorox Co. (The)			1,100	45,485

See accompanying notes to the financial statements.

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PROGRESSIVE RETURN FUND, INC.
CORNERSTONE STRATEGIC VALUE FUND, INC.
SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

Description	CORNERSTONE STRATEGIC VALUE FUND, INC. Principal Amount (000's)	Value	PROGRESSIVE R FUND, INC. Principal Amount (000's)	Value
Coca-Cola Co. (The)	9,000	504,000	8,800	492,800
Coca-Cola Enterprises Inc.			2,500	55,200
Colgate-Palmolive Co.	2,000	100,100	2,600	130,130
ConAgra Foods, Inc.	1,900	52,535	2,500	69,125
General Mills, Inc.			1,300	57,304
Gillette Co. (The)	3,800	128,706	3,000	101,610
H.J. Heinz Co.			1,600	65,760
J.M. Smucker Co. (The)	96	3,276	70	2,389
Kellogg Co.			1,900	68,134
Kimberly-Clark Corp.	1,900	117,800	2,500	155,000
Kroger Co. (The)			1,300	25,870
PepsiCo, Inc.	5,100	245,820		
Philip Morris Companies Inc.	7,900	345,072	6,900	301,392
Proctor & Gamble Co. (The)	4,800	428,640		
Safeway Inc.			2,500	72,975
Sara Lee Corp.	2,800	57,792	3,800	78,432
Sysco Corp.	65,800	1,791,076	3,100	84,382
Unilever NV, NY Shares	2,000	129,600	2,000	129,600
Walgreen Co.			4,600	177,698
Wm. Wrigley Jr. Co.			1,100	60,885
		4,095,305		2,411,125
ENERGY - 7.76%				
Andarko Petroleum Corp.	900	44,370	1,200	59,160
Baker Hughes Inc.	2,500	83,225	1,100	36,619
Burlington Resources Inc.			1,000	38,000
ChevronTexaco Corp.	7,840	693,840	4,325	382,762
Conoco Inc.	2,200	61,160	2,800	77,840
El Paso Corp.	2,500	51,525	2,500	51,525
Exxon Mobil Corp.	15,400	630,168	19,800	810,216
Marathon Oil Corp.	2,500	67,800	1,500	40,680
Occidental Petroleum Corp.	2,500	74,975	1,700	50,983
Phillips Petroleum Co.	2,500	147,200	1,200	70,656
Royal Dutch Petroleum Co., NY Shares	7,500	414,525	6,300	348,201
Schlumberger Ltd.	2,000	93,000	2,600	120,900
			1,200	44,328
		2,361,788		2,131,870
FINANCIALS - 16.71%				
AFLAC Inc.	1,900	60,800	2,600	83,200
Allstate Corp. (The)			3,300	122,034
American Express Co.	4,600	167,072	4,100	148,912
American International Group, Inc.	11,542	787,511	5,989	408,629
AmSouth Bancorporation			1,800	40,284
Aon Corp.			1,200	35,376
Bank of America Corp.	5,400	379,944		
Bank of New York Co., Inc. (The)			3,400	114,750

Bank One Corp.	4,100	157,768	2,800	107,744
BB&T Corp.	1,600	61,760		
Charles Schwab Corp. (The)			3,500	39,200
Charter One Financial, Inc.			1,050	36,099
Citigroup Inc.	17,100	662,625	16,500	639,375
Fannie Mae	3,700	272,875	1,500	110,625
Fifth Third Bancorp.	2,000	133,300	2,500	166,625
FleetBoston Financial Corp.	3,900	126,165	4,100	132,635
Franklin Resources, Inc.			1,200	51,168
Freddie Mac	2,500	153,000	3,100	189,720
H&R Block Inc.			1,000	46,150
Hartford Financial Services Group, Inc. (The)	2,500	148,675	1,000	59,470
Household International, Inc.	1,800	89,460	2,500	124,250
Huntington Banschares Inc.			1,200	23,304
J.P. Morgan Chase & Co.	6,000	203,520	6,200	210,304

See accompanying notes to the financial statements.

PROGRESSIVE RETURN FUND, INC.
CORNERSTONE STRATEGIC VALUE FUND, INC.
SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

	CORNERSTONE STRATEGIC VALUE FUND, INC.		PROGRESSIVE R FUND, INC.	
Description	Principal Amount (000's)	Value	Principal Amount (000's)	Value
Lehman Brothers Holdings Inc.			1,100	68,772
Marsh & McLennan Companies, Inc.	2,000	193,200	1,300	125,580
MBNA Corp.	3,000	99,210	1,400	46,298
Mellon Financial Corp.	1,800	56,574	2,500	78,575
Merrill Lynch & Co., Inc.			3,700	149,850
MetLife, Inc.	2,700	77,760	3,500	100,800
Morgan Stanley	7,000	301,560	2,500	107,700
National City Corp.	2,200	73,150		
Northern Trust Corp.			1,000	44,060
PNC Financial Services Group	1,100	57,508		
Regions Financial Corp.			1,000	35,150
SouthTrust Corp.	2,500	65,300		
State Street Corp.	2,500	111,750		
St. Paul Companies, Inc. (The)			1,000	38,920
SunTrust Banks, Inc.	1,100	74,492		
Synovus Financial Corp.			1,300	35,776
UnumProvident Corp.			1,100	27,995
U.S. Bancorp.	6,700	156,445	6,201	144,793
Wachovia Corp.	3,600	137,448	4,000	152,720
Washington Mutual, Inc.	3,150	116,897	3,750	139,163
Wells Fargo & Co.	5,800	290,348	5,400	270,324
		5,216,117		4,456,330

HEALTH CARE - 12.76%				
Abbott Labratories	5,300	199,545	5,000	188,250
Allergan, Inc.			1,000	66,750
Amgen Inc.*			3,300	138,204
Baxter International Inc.	2,500	111,100	2,800	124,432
Becton, Dickinson & Co.			1,200	41,340
Boston Scientific Corp.*	2,500	73,300	2,500	73,300
Bristol-Myers Squibb Co.			6,400	164,480
Cardinal Health, Inc.	2,500	153,525	1,950	119,750
Eli Lilly & Co.	4,000	225,600	2,800	157,920
Genzyme Corp. *	2,500	48,100	2,500	48,100
Guidant Corp.			1,400	42,322
HCA Inc.	2,000	95,000	2,500	118,750
Healthsouth Corp.*	2,500	31,975	1,800	23,022
Johnson & Johnson	9,200	480,792	9,778	510,998
McKesson Corp.			1,300	42,510
MedImmune, Inc.*			1,000	26,400
Medtronic, Inc.	4,300	184,255	3,000	128,550
Merck & Co. Inc.	2,500	126,600	10,500	531,720
Pfizer Inc.	37,000	1,295,000	15,100	528,500
Pharmacia Corp.			3,400	127,330
Schering-Plough Corp.	2,500	61,500	4,200	103,320
Tenet Healthcare Corp.			1,500	107,325
UnitedHealth Group Inc.	2,500	228,875	1,500	137,325
Wyeth	4,800	245,760	4,200	215,040
Zimmer Holdings, Inc.*	710	25,319	890	31,737
		3,586,246		3,797,375
INDUSTRIALS - 10.49%				
3M Co.	1,500	184,500	1,900	233,700
Automatic Data Processing, Inc.	2,000	87,100	2,900	126,295
Boeing Co. (The)	6,000	270,000		
Burlington Northern Sante Fe Corp.	2,500	75,000	1,900	57,000
Caterpillar Inc.	1,300	63,635	1,600	78,320
Cendant Corp.*	2,700	42,876	3,300	52,404
Concord EFS, Inc.*	2,500	75,350	2,500	75,350
CSX Corp.			1,000	34,810
Deere & Co.			1,100	52,690
Emerson Electric Co.	1,500	80,265	2,000	107,020

See accompanying notes to the financial statements.

PROGRESSIVE RETURN FUND, INC.
CORNERSTONE STRATEGIC VALUE FUND, INC.
SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

CORNERSTONE STRATEGIC VALUE FUND, INC.	PROGRESSIVE R FUND, INC.

Description	Principal Amount (000's)	Value	Principal Amount (000's)	Value
FedEx Corp.	1,000	53,400	1,300	69,420
First Data Corp.	5,000	188,300	3,800	143,108
General Dynamics Corp.			600	63,810
General Electric Co.	34,500	1,002,225	28,700	833,735
Honeywell International Inc.	2,800	98,644	3,600	126,828
Illinois Tool Works Inc.			1,400	96,488
Imagistics International Inc.*			88	1,889
IMS Health Inc.			1,400	25,130
Ingersoll-Rand Co., Class A			1,000	45,660
Masco Corp.	1,700	46,087	2,500	67,775
Norfolk Southern Corp.	1,400	32,732	1,800	42,084
Paychex, Inc.	2,500	78,225	1,700	53,193
Pitney Bowes Inc.			1,100	43,692
Raytheon Co.			1,600	65,200
Southwest Airlines Co.	2,700	43,632	3,750	60,600
Tyco International Ltd.	12,500	168,875	6,397	86,423
Union Pacific Corp.	1,000	63,280	1,100	69,608
United Technologies Corp.	4,200	285,180	2,500	169,750
Vivendi Universal SA, ADR			2,500	53,750
Waste Management, Inc.	4,700	122,435	2,800	72,940
		3,061,741		3,008,672
INFORMATION TECHNOLOGY - 12.41%				
Adobe Systems Inc.			1,100	31,350
Agere Systems Inc., Class B*	2,831	4,246	3,069	4,604
Agilent Technologies, Inc.*	1,800	42,984		
Altera Corp.			1,900	25,840
Analog Devices, Inc.*	10,000	297,000	1,700	50,490
Apple Computer, Inc.*	2,500	44,300	1,500	26,580
Applied Materials, Inc.*	5,400	102,708	7,400	140,748
Cisco Systems, Inc.*	24,400	340,380	23,500	327,825
Computer Associates International, Inc.	2,500	39,725	2,700	42,903
Compuware Corp.			1,700	10,319
Conexant Systems, Inc.			1,100	1,782
Dell Computer Corp.*	8,300	216,962		
Electronic Data Systems Corp.			2,500	92,875
Hewlett-Packard Co.	2,800	42,784	8,100	123,768
Intel Corp.	26,000	475,020	21,600	394,632
International Business Machines Corp.	8,400	604,800	5,500	396,000
Intuit Inc.*			2,000	99,440
Linear Technology Corp.			1,500	47,145
LSI Logic Corp.*			1,500	13,125
Lucent Technologies Inc.*	10,700	17,762	11,600	19,256
Maxim Integrated Products, Inc.*			1,300	49,829
Micron Technology, Inc.*			2,600	52,572
Microsoft Corp.*	20,600	1,114,872	17,300	936,276
Motorola, Inc.	6,600	95,172	7,100	102,382
NVIDIA Corp.			1,000	17,180
Oracle Corp.*	6,300	59,661	17,800	168,566
PerkinElmer, Inc.			1,000	11,050
QUALCOMM Inc.*			1,500	41,235
Sanmina-SCI Corp.*	2,500	15,775	3,000	18,930

Description	Principal Amount (000's)	Value	Principal Amount (000's)	Value
Siebel Systems, Inc.*	2,500	35,550		
Skyworks Solutions, Inc.*			386	2,143
Solectron Corp.*			3,700	22,755
Sun Microsystems, Inc.*			10,000	50,100
Texas Instruments Inc.	4,900	116,130	5,400	127,980
Yahoo! Inc.*	1,900	28,044	2,500	36,900
		3,693,875		3,486,580
MATERIALS - 2.82%				
Air Products & Chemicals, Inc.	1,000	50,470	1,100	55,517
Alcan Inc.			1,500	56,280
Alcoa Inc.	3,100	102,765	4,200	139,230

See accompanying notes to the financial statements.

PROGRESSIVE RETURN FUND, INC.
CORNERSTONE STRATEGIC VALUE FUND, INC.
SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

	CORNERSTONE STRATEGIC VALUE FUND, INC.		PROGRESSIVE R FUND, INC.	
Description	Principal Amount (000's)	Value	Principal Amount (000's)	Value
Barrick Gold Corp.	2,500	47,475	2,589	49,165
Dow Chemical Co. (The)	5,700	195,966	4,100	140,958
E.I. du Pont de Nemours & Co.	3,700	164,280	3,300	146,520
Georgia-Pacific Corp.	1,000	24,580	1,000	24,580
Inco Ltd.*	2,500	56,675		
International Paper Co.	2,000	87,160	2,500	108,950
Placer Dome Inc.			1,500	16,815
Rohm and Haas Co.			1,000	40,490
Weyerhaeuser Co.	1,000	63,850	1,000	63,850
		793,221		842,355
TELECOMMUNICATION SERVICES - 4.37%				
Alcatel SA, ADR			8,400	59,724
ALLTEL Corp.	2,500	117,500	1,500	70,500
AT&T Corp.	5,000	53,500	11,300	120,910
AT&T Wireless Services Inc.*	3,022	17,679	5,534	32,374
BellSouth Corp.	4,000	126,000	6,000	189,000
SBC Communications Inc.	19,900	606,950	10,700	326,350
Sprint Corp. (FON Group)	3,000	31,830	4,000	42,440
Sprint Corp. (PCS Group)			1,800	8,046
Verizon Communications Inc.	9,400	377,410	8,700	349,305

		1,330,869		1,198,649
UTILITIES - 2.65%				
American Electric Power Co., Inc.	1,200	48,024	1,500	60,030
Consolidated Edison, Inc.			1,000	41,750
Dominion Resources, Inc.	1,000	65,980	1,100	72,578
Duke Energy Corp.	5,600	174,160	2,500	77,750
Edison International*	2,500	42,500	1,500	25,500
Entergy Corp.			1,100	46,684
Exelon Corp.			1,500	78,450
FirstEnergy Corp.	2,500	83,450	1,100	36,718
Mirant Corp.*			1,232	8,994
NiSource Inc.			1,000	21,830
PG&E Corp.*			1,800	32,202
Progress Energy, Inc.			1,000	52,010
Public Service Enterprises Group Inc.			1,000	43,300
Reliant Energy, Inc.	2,500	42,250	1,400	23,660
Scottish Power plc ADR	4,000	85,600		
Sempra Energy			1,000	22,130
Southern Co. (The)	2,400	65,760	3,100	84,940
TXU Corp.	1,000	51,400	1,200	61,680
Williams Companies, Inc. (The)			2,500	14,975
Xcel Energy, Inc.	2,500	41,925	1,600	26,832
		701,049		832,013
TOTAL EQUITY SECURITIES (cost - $28,336,352, $32,698,482 and $61,034,834, respectively		$28,851,286		$26,749,790
			Principal Amount (000's)	
FIXED INCOME SECURITIES - 2.49%				
U.S. GOVERNMENT OBLIGATIONS - 2.49%				
U.S. TREASURY NOTES - 2.49%				
3.00%, 01/31/04			$ 500	503,260
4.75%, 02/15/04			500	517,244
5.25%, 05/15/04			400	418,074
TOTAL FIXED INCOME SECURITIES (cost - $0, $1,439,859 and $1,439,859)				1,438,578

See accompanying notes to the financial statements.

SCHEDULE OF INVESTMENTS - JUNE 30, 2002 (UNAUDITED)

Description	CORNERSTONE STRATEGIC VALUE FUND, INC. Principal Amount (000's)	Value	PROGRESSIVE R FUND, INC. Principal Amount (000's)	Value
SHORT-TERM INVESTMENT - 1.55%				
REPURCHASE AGREEMENT - 1.55%				
Bear, Stearns & Co. Inc. (Agreement dated 06/30/02 to be repurchased at $622,242), 1.92%, 07/03/02 (cost - $609,778, $287,570 and $897,348, respectively	$610	609,778	$ 288	287,570
TOTAL INVESTMENTS - 100.10% (cost - $28,946,130, 34,425,911 and $63,372,041, respectively		29,461,064		28,475,938
LIABILITIES IN EXCESS OF CASH AND OTHER ASSETS - (0.10)%		(47,288)		(10,942)
NET ASSETS - 100.00%		$ 29,413,776		$28,464,996

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STATEMENT OF OPERATIONS
FOR THE SIX MONTHS ENDED JUNE 30, 2002(UNAUDITED)

	PGF ACQUIRING FUND	CLM	ADJUSTM
INVESTMENT INCOME			
Income:			
Dividends	$ 255,396.0	$ 236,248	
Interest	6,045	3,925	
Less: Foreign taxes witheld	(1,254)	(1,241)	

Total Investment Income	260,187	238,932	
Expenses:			
Investment advisory fees	175,390	164,694	$ (53
Audit fees	6,500	6,500	(6
Legal fees	46,309	39,834	(44
Administration fees	24,795	24,795	(20
Custodian fees	5,439	4,570	(3
Printing	18,348	17,900	(13
Accounting fees	15,048	14,516	(13
Directors' fees	31,891	25,491	(31
Transfer agent fees	14,760	3,571	(6
NYSE listing fees	13,986	13,820	(15
Insurance	4,240	5,992	
Merger	--	--	137
Other	8,944	3,545	(6
Total Expenses	365,650	325,228	(79
Less: Fee paid indirectly	(18,365)	(10,332)	
Net Expenses	347,285	314,896	(79
Net Investment Income	(87,098)	(75,964)	79
NET REALIZED AND UNREALIZED GAIN/(LOSS) ON INVESTMENTS			
Net realized loss from Investments	(1,057,403)	(1,081,463)	
Net change in unrealized appreciation/(depreciation) in value of investments	(4,030,577)	(4,474,326)	
Net realized and unrealized gain/(loss) on investments	(5,087,980)	(5,555,789)	
NET INCREASE IN NET ASSETS RESULTING FROM OPERATIONS	$ (5,175,078)	$ (5,631,753)	$ 79

See accompanying notes to financial statements.

STATEMENT OF ASSETS AND LIABILITIES
AT JUNE 30, 2002 (UNAUDITED)

	PGF ACQUIRING FUND	
ASSETS	COST	VALUE

Investments, at value	$ 34,425,911	$ 28,475,938
Cash collateral received for securities loaned		167,478
Receivables:		
Dividends		35,183
Interest		18,624
Prepaid expenses and other assets		17,395
Total Assets		28,714,618
LIABILITIES		
Payables:		
Upon return of securities loaned		167,478
Investment advisory fee		24,230
Capital Shares repurchased		--
Other accrued expenses		57,914
Total Liabilities		249,622
Net Assets		$ 28,464,996
Net Assets Consist Of:		
Capital stock, $0.004 par value; 1,147,786 shares issued and outstanding for PGF (100,000,000 shares authorized) and $0.01 par value; 3,805,860 shares issued and outstanding for CLM (25,000,000 shares authorized)	$ 4,591	$ 38,059
Paid-in-capital	62,788,936	57,277,380
Cost of 0 and 2,204,140 shares repurchased, respectively	--	(26,790,440)
Accumulated/Distribution in excess of net investment income	(15,149,979)	(75,964)
Accumulated net realized loss on investments	(13,228,579)	(1,550,193)
Net unrealized appreciation/(deprecation) in value of investments	(5,949,973)	514,934
Net assets applicable to shares outstanding	$ 28,464,996	$ 29,413,776
Net Asset Value Per Share	$ 24.80	$ 7.73
Shares Outstanding		

	PGF ADJUSTMENTS	PRO FORMA COST
Investments, at value		$ 63,372,041
Cash collateral received for securities loaned		
Receivables:		
Dividends		
Interest		

Prepaid expenses and other assets	$ (33,057)(a)	
Total Assets		
LIABILITIES		
Payables:		
Upon return of securities loaned		
Investment advisory fee		
Capital Shares repurchased		
Other accrued expenses	137,160(b)	
Total Liabilities		
Net Assets		
Net Assets Consist Of:		
Capital stock, $0.004 par value; 1,147,786 shares issued and outstanding for PGF (100,000,000 shares authorized) and $0.01 par value; 3,805,860 shares issued and outstanding for CLM (25,000,000 shares authorized)		
Paid-in-capital		(26,790,440)(c)
Cost of 0 and 2,204,140 shares repurchased, respectively		26,790,440(c)
Accumulated/Distribution in excess of net investment income		(170,217)(a)(
Accumulated net realized loss on investments		
Net unrealized appreciation/(deprecation) in value of investments		
Net assets applicable to shares outstanding		
Net Asset Value Per Share		
Shares Outstanding		

See accompanying notes to financial statements.

Progressive Return Fund, Inc.
The Cornerstone Strategic Value, Inc.
Notes to Pro Forma Financial Statements (unaudited)

1. Basis of Combination

The unaudited Pro Forma Condensed Portfolio of Investments, Pro Forma Condensed Statement of Assets and Liabilities and Pro Forma Condensed Statement of Operations give effect to the proposed merger of Cornerstone Strategic Value

Fund, Inc.("CLM") into Progressive Return Fund, Inc. ("PGF"). The proposed merger will be accounted for by the method of accounting for tax-free mergers of investment companies (sometimes referred to as the pooling-of-interest basis). The Merger provides for the transfer of all or substantially all of the assets of CLM to PGF in exchange for PGF common shares, the distribution of such PGF common shares to common shareholders of CLM and the subsequent liquidation of CLM. Each share of common stock of CLM will convert into an equivalent dollar amount of full shares of common stock of PGF based on the net asset value per share of each Fund.

The pro forma combined statements should be read in conjunction with the historical financial statements of the constituent Fund and the notes thereto incorporated by reference in the Registration Statement filed on Form N-14.

PGF and CLM are both closed-end, non-diversified and diversified management investment companies, respectively, registered under the Investment Company Act of 1940, as amended.

Pro Forma Adjustments:

The Pro Forma adjustments below reflect the impact of the merger between PGF and CLM.

(a) To remove certain prepaid expenses associated with CLM, in the statement of assets and liabilities, which will not be assumed by PGF.

(b) Adjustment for expenses relating to the merger.

(c) In connection with CLM's intention to merge with PGF; CLM reclass its shares repurchased to paid-in capital.

(d) Adjustment based on contractual agreement with Investment Manager.

(e) Assumes the elimination of duplicative charges resulting from the combination and reflects management's estimates of combined pro forma operations.

(f) Adjustment based on the contractual agreement with the Administrator for the combined Fund.

(g) Adjustment based on the contractual agreement with the custodian for the combined Fund.

(h) Adjustment based on the contractual agreement with the Accounting fees for the combined Fund.

2. SIGNIFICANT ACCOUNTING POLICIES

The following is a summary of significant accounting policies, which are consistently followed by each of PGF and CLM in the preparation of its financial statements.

MANAGEMENT ESTIMATES: The preparation of financial statements in accordance with ccounting principles generally accepted in the United States of

America requires management to make certain estimates and assumptions that may affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates.

PORTFOLIO VALUATION: Investments are stated at value in the accompanying financial statements. All equity securities are valued at the closing price on the exchange or market on which the security is primary traded ("Primary Market"). If the security did not trade on the Primary Market, it shall be valued at the closing price on another exchange where it trades. If there is no such sale prices, the value shall be the most recent bid. If no pricing service is available and there are more than two dealers, the value shall be the mean of the highest bid and lowest ask. If there is only one dealer, then the value shall be the mean if bid and ask are available, otherwise the value shall be the bid.

All other securities and assets are valued as determined in good faith by the Board of Directors. Short-term investments having a maturity of 60 days or less are valued on the basis of amortized cost. The Board of Directors has established general guidelines for calculating fair value of not readily marketable securities. The net asset value per share of each Fund is calculated weekly and on the last business day of the month with the exception of those days on which the New York Stock Exchange is closed.

INVESTMENT TRANSACTIONS AND INVESTMENT INCOME: Investment transactions are accounted for on the trade date. The cost of investments sold is determined by use of the specific identification method for both financial reporting and income tax purposes. Interest income is recorded on an accrual basis; dividend income is recorded on the ex-dividend date.

TAXES: No provision is made for U.S. federal income or excise taxes as it is each Fund's intention to continue to qualify as a regulated investment company and to make the requisite distributions to its shareholders which will be sufficient to relieve it from all or substantially all U.S. federal income and excise taxes.

DISTRIBUTIONS OF INCOME AND GAINS: Each Fund distributes at least annually to shareholders, substantially all of its net investment income and net realized short-term capital gains, if any. Each Fund determines annually whether to distribute any net realized long-term capital gains in excess of net short-term capital losses, including capital loss carryovers, if any. An additional distribution may be made to the extent necessary to avoid the payment of a 4% U.S. federal excise tax. Dividends and distributions to shareholders are recorded by each Fund on the ex-dividend date. .

The board of Directors of each Fund may, if it it determined to be in the best interest of each Fund and its shareholders, time to time authorize and declare distribution that may be substantially characterized as a return of capital.

The character of distributions made during the year from net investment income or net realized gains may differ from their ultimate characterization for U.S. federal income tax purposes due to U.S. generally accepted accounting principles/tax differences in the character of income and expense recognition.

OTHER: Securities denominated in currencies other than U.S. dollars are subject to changes in value due to fluctuations in exchange rates.

EXHIBIT A

MERGER AGREEMENT AND PLAN OF REORGANIZATION

THIS MERGER AGREEMENT AND PLAN OF REORGANIZATION (the "Agreement") is made as of this 11th day of October, 2002, between Cornerstone Strategic Value Fund, Inc. (the "Target Fund" or "CLM"), a Maryland corporation and a registered investment company under the Investment Company Act of 1940, as amended (the "1940 Act"), and Progressive Return Fund, Inc. (the "Acquiring Fund" or "PGF"), a Maryland corporation and a registered investment company under the 1940 Act.

This agreement contemplates a tax-free merger transaction which qualifies for federal income tax purposes as a reorganization within the meaning of Section 368(a)(1)(A) of the Internal Revenue Code of 1986, as amended (the "Code").

NOW, THEREFORE, in consideration of the covenants and agreements hereinafter set forth, the Parties hereto agree as follows:

1. DEFINITIONS

Certain capitalized terms used in this Agreement are specifically defined herein.

2. BASIC TRANSACTION

2.1. THE MERGER. On and subject to the terms and conditions of this Agreement, the Target Fund will merge with and into the Acquiring Fund (the "Merger") at the Effective Date (as defined in Section 2.3 below) in accordance with the Maryland General Corporation Law ("MGCL"). PGF shall be the surviving investment company. CLM shall cease to exist as a separate investment company.

Each share of common stock of CLM will be converted into shares of Common Stock of PGF in accordance with Section 5.01 below.

2.2. ACTIONS AT CLOSING. At the closing of the transactions contemplated by this Agreement (the "Closing") on the date thereof (the "Closing Date"), (i) CLM will deliver to PGF the various certificates and documents referred to in Article 7 below, (ii) PGF will deliver to CLM the various certificates and documents referred to in Article 8 below, and (iii) CLM and PGF will file jointly with the State Department of Assessments and Taxation of Maryland (the "Department") articles of merger (the "Articles of Merger") and make all other filings or recordings required by Maryland law in connection with the Merger.

2.3. EFFECT OF MERGER. Subject to the requisite approvals of the shareholders of the Parties, and to the other terms and conditions described herein, the Merger shall become effective at such time as the Articles of Merger

are accepted for record by the Department or at such later time as is specified in the Articles of Merger (the "Effective Date") and the separate corporate existence of CLM shall cease. As promptly as practicable after the Merger, CLM shall delist its shares from the NYSE and its registration under the 1940 Act shall be terminated. Any reporting responsibility of CLM is, and shall remain, the responsibility of CLM up to and including the Effective Date.

3. REPRESENTATIONS AND WARRANTIES OF CLM

CLM represents and warrants to PGF that the statements contained in this Article 3 are correct and complete in all material respects as of the execution of this Agreement on the date hereof. CLM represents and warrants to, and agrees with, PGF that:

3.1. ORGANIZATION. CLM is a corporation duly organized, validly existing under the laws of the State of Maryland and is in good standing with the Department, and has the power to own all of its assets and to carry on its business as it is now being conducted and to carry out this Agreement.

3.2. REGISTRATIONS AND QUALIFICATIONS. CLM is duly registered under the 1940 Act as a closed-end, diversified management investment company (File No. 005-39655), and such registration has not been revoked or rescinded and is in full force and effect. CLM has elected and qualified for the special tax treatment afforded regulated investment companies ("RIC") under Sections 851-855 of the Code at all times since its inception. CLM is qualified as a foreign corporation in every jurisdiction where required, except to the extent that failure to so qualify would not have a material adverse effect on CLM.

3.3. REGULATORY CONSENTS AND APPROVALS. No consent, approval, authorization, or order of any court or governmental authority is required for the consummation by CLM of the transactions contemplated herein, except (i) such as have been obtained or applied for under the Securities Act of 1933, as amended (the "1933 Act"), the Securities Exchange Act of 1934 (the "1934 Act"), and the 1940 Act, (ii) such as may be required by state securities laws and (iii) such as may be required under Maryland law for the acceptance for record of the Articles of Merger by the Department.

3.4. NONCONTRAVENTION. CLM is not, and the execution, delivery and performance of this Agreement by CLM will not result in, a violation of the laws of the State of Maryland or of the Articles of Incorporation or the By-laws of CLM, or of any material agreement, indenture, instrument, contract, lease or other undertaking to which CLM is a party or by which it is bound, and the execution, delivery and performance of this Agreement by CLM will not result in the acceleration of any obligation, or the imposition of any penalty, under any agreement, indenture, instrument, contract, lease, judgment or decree to which CLM is a party or by which it is bound.

3.5. FINANCIAL STATEMENTS. PGF has been furnished with CLM's Annual Report of Stockholders, as of December 31, 2001, said financial statements having been examined by PricewaterhouseCoopers LLP, independent public auditors. These financial statements are in accordance with generally accepted accounting principles applied on a consistent basis ("GAAP") and present fairly, in all material respects, the financial position of CLM as of such date in accordance with GAAP, and there are no known contingent liabilities of CLM required to be reflected on a balance sheet (including the notes thereto) in accordance with GAAP as of such date not disclosed therein.

PGF has also been furnished with CLM's Semi-Annual Report to Stockholders dated as of June 30, 2002. This financial statement and the schedule of investments are in accordance with GAAP and present fairly, in all material respects, the financial position of CLM as of such date in accordance with GAAP, and there are no known contingent liabilities of CLM required to be

reflected on a balance sheet (including the notes thereto) in accordance with GAAP as of such date not disclosed therein.

3.6. This Section has been left intentionally Blank.

3.7. QUALIFICATION, CORPORATE POWER, AUTHORIZATION OF TRANSACTION. CLM has full power and authority to enter into and perform its obligations under this Agreement. The execution, delivery and performance of this Agreement has been duly authorized by all necessary action of its Board of Directors, and, subject to shareholder approval, this Agreement constitutes a valid and binding contract enforceable in accordance with its terms, subject to the effects of bankruptcy, insolvency, moratorium, fraudulent conveyance and similar laws relating to or affecting creditors' rights generally and court decisions with respect thereto.

3.8. LEGAL COMPLIANCE. No material litigation or administrative proceeding or investigation of or before any court or governmental body is presently pending (in which service of process has been received) or to its knowledge threatened against CLM or any properties or assets held by it. CLM knows of no facts which might form the basis for the institution of such proceedings which would materially and adversely affect its business and is not a party to or subject to the provisions of any order, decree or judgment of any court or governmental body which materially and adversely affects its business or its ability to consummate the transactions herein contemplated.

3.9. MATERIAL CONTRACTS. There are no material contracts outstanding to which CLM is a party that have not been disclosed in the N-14 Registration Statement (as defined in Section 3.13 below) or will not be otherwise disclosed to PGF prior to the Effective Date.

3.10. UNDISCLOSED LIABILITIES. There has not been any material adverse change in CLM's financial condition, assets, liabilities or business and CLM has no known liabilities of a material amount, contingent or otherwise, required to be disclosed in a balance sheet in accordance with GAAP other than those shown on CLM's statements of assets, liabilities and capital referred to above, those incurred in the ordinary course of its business as an investment company, and those incurred in connection with the Merger. Prior to the Effective Date, CLM will advise PGF in writing of all known liabilities,

contingent or otherwise, whether or not incurred in the ordinary course of business, existing or accrued. For purposes of this Section 3.10, a decline in net asset value per share of CLM due to declines in market values of securities in CLM's portfolio or the discharge of CLM liabilities will not constitute a material adverse change.

3.11. TAX FILINGS. All federal and other tax returns and information reports of CLM required by law to have been filed shall have been filed and are or will be correct in all material respects, and all federal and other taxes shown as due or required to be shown as due on said returns and reports shall have been paid or provision shall have been made for the payment thereof, and, to the best of CLM's knowledge, no such return is currently under audit and no assessment has been asserted with respect to such returns. All tax liabilities of CLM have been adequately provided for on its books, and no tax deficiency or liability of CLM has been asserted and no question with respect thereto has been raised by the Internal Revenue Service or by any state or local tax authority for taxes in excess of those already paid, up to and including the taxable year in which the Effective Date occurs.

3.12. QUALIFICATION UNDER SUBCHAPTER M. For each taxable year of its operation (including the taxable year ending on the Effective Date), CLM has met the requirements of Subchapter M of the Code for qualification as a RIC and has elected to be treated as such, has been eligible to and has computed its federal income tax under Section 852 of the Code, and will have distributed substantially all of its investment company taxable income and net realized capital gain (as defined in the Code) that has accrued through the Effective Date.

3.13. FORM N-14.The registration statement to be filed by PGF on Form N-14 relating to PGF common stock to be issued pursuant to this Agreement, and any supplement or amendment thereto or to the documents therein, as amended (the "N-14 Registration Statement"), on the effective date of the N-14 Registration Statement, at the time of the shareholders' meetings referred to in Article 6 of this Agreement and at the Effective Date, insofar as it relates to CLM (i) shall have complied or will comply in all material respects with the provisions of the 1933 Act, the 1934 Act and the 1940 Act and the rules and regulations thereunder and (ii) did not or will not contain any untrue statement of a material fact or omit to state any material fact required to be stated therein or necessary to make the statements therein not misleading; and the prospectus included therein did not or will not contain any untrue statement of a material fact or omit to state any material fact necessary to make the statements therein, in light of the circumstances under which they were made, not misleading; provided, however, that the representations and warranties in this Section 3.13 shall only apply to statements in, or omissions from, the N-14 Registration Statement made in reliance upon and in conformity with information furnished by PGF for use in the N-14 Registration Statement.

3.14. CAPITALIZATION.

(a) All issued and outstanding shares of CLM (i) have been offered and sold in compliance in all material respects with applicable registration requirements of the 1933 Act and state securities laws, (ii) are, and on the Effective Date will be, duly and validly issued and outstanding, fully paid and non-assessable, and (iii) will be held at the time of the Closing by the persons and in the amounts set forth in the records of the transfer agent as provided in Section 6.7. CLM does not have outstanding any options, warrants or other rights to subscribe for or purchase any of CLM shares, nor is there outstanding any security convertible into, or exchangeable for, any of CLM shares.

(b) CLM is authorized to issue 25,000,000 shares of stock, par value $0.01 per share, all of which shares are classified as common stock and each outstanding share of which is fully paid, non-assessable and has full voting rights.

3.15. BOOKS AND RECORDS. The books and records of CLM made available to PGF are substantially true and correct and contain no material misstatements or omissions with respect to the operations of CLM.

4. REPRESENTATIONS AND WARRANTIES OF PGF

PGF represents and warrants to CLM that the statements contained in this Article 4 are correct and complete in all material respects as of the execution of this Agreement on the date hereof. PGF represents and warrants to, and agrees with, CLM that:

4.1. ORGANIZATION. PGF is a corporation duly organized, validly existing under the laws of the State of Maryland and is in good standing with the Department, and has the power to own all of its assets and to carry on its business as it is now being conducted and to carry out this Agreement.

4.2. REGISTRATIONS AND QUALIFICATIONS. PGF is duly registered under the 1940 Act as a closed-end, diversified management investment company (File No. 005-40528) and such registration has not been revoked or rescinded and is in full force and effect. PGF has elected and qualified for the special tax treatment afforded RICs under Sections 851-855 of the Code at all times since its inception. PGF is qualified as a foreign corporation in every jurisdiction where required, except to the extent that failure to so qualify would not have a material adverGN="RIGHT">2,135

Three-for-Two Stock Split 2005

234

234

22

22

(256
)

Unearned Compensation

152

152

3,701

(3,368
)

485

Other

318

318

(2
)

(2
)

1,397

1,713

Balance at December 31, 2004

69,060

$
69,060

(556
)
$
(556
)
$
7,419

$
3,240

$

$
(16,066
)
$
(3,475
)
$
107,927

$
167,549

Net Income

52,773

52,773

52,773

Other Comprehensive Income, Net of Tax

Minimum Pension Liability Adjustment

(8,181
)

(8,181
)

Foreign Currency Translation Adjustments

1,114

1,114

NSO Stock Options

(131
)

(131
)

Other Comprehensive Income

(7,198
)

(7,198
)

Comprehensive Income

$
45,575

Cash Dividends

(13,714
)

(13,714
)

Common Stock Purchased (2)

(1,438
)

(1,438
)

(5,349
)

(23,446
)

(30,233
)

Issuance of 401(k) Company Match

90

90

2,109

2,199

Three-for-Two Stock Split 2005

68

68

(164
)

(164
)

10

86

Unearned Compensation

146

146

3,490

(2,406
)

(5
)

1,225

Common Stock Options Exercised

805

805

2,523

3,328

Non-Qualified Stock Options

1,022

1,022

Balance at December 31, 2005

70,079

$
70,079

(2,068
)
$
(2,068
)
$
14,464

$

$

$
(23,264
)
$
(5,881
)
$
123,621

$
176,951

Net Income

57,809

57,809

57,809

Other Comprehensive Income, Net of Tax

Minimum Pension Liability Adjustment

5,717

5,717

Foreign Currency Translation Adjustments

(237
)

(237
)

Other Comprehensive Income

5,480

5,480

Comprehensive Income

$
63,289

Cash Dividends

(17,025
)

(17,025
)

Common Stock Purchased (2)

(1,007
)

(1,007
)

(3,655
)

(14,790
)

(19,452
)

Issuance of 401(k) Company Match

177

177

3,655

3,832

FAS 123r Adoption

(5,881
)

5,881

Stock Compensation

281

281

2,755

3,036

Common Stock Options Exercised & Other

429

429

399

828

Balance at December 31, 2006

70,789

$
70,789

(2,898
)
$
(2,898
)
$
11,737

$

$

$
(17,784

)
$

$
149,615

$
211,459

(1) Includes translation adjustment (net of tax) of $1,683,000 relating to non-current assets as of December 31, 2003.

(2) Charged to Retained Earnings are from purchases of the Company's Common Stock.

The accompanying notes are an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

Rollins, Inc. and Subsidiaries

Years ended December 31, (in thousands)	2006	2005	2004
OPERATING ACTIVITIES			
Net Income	**$ 57,809**	$ 52,773	$ 52,055
Adjustments to reconcile net income to net cash			
Provided by operating activities:			
Change in accounting principle, net			6,204
Depreciation and amortization	**26,860**	24,280	23,034
Pension curtailment		(4,176)	
Provision for deferred income taxes	**6,007**	3,653	13,078
Stock Based Compensation Expense	**1,830**	739	260
Gain on sales of assets	**(81)**	(982)	(24,716)
Other, net	**(544)**	(2,834)	295
(Increase)/decrease in assets			
Trade receivables	**(3,784)**	4,291	(6,088)
Materials and supplies	**681**	2,385	2,645
Other current assets	**1,914**	715	482
Other non-current assets	**301**	353	(632)
Increase/(decrease) in liabilities:			
Accounts payable and accrued expenses	**6,633**	4,893	16,588
Unearned revenue	**(550)**	(31)	5,582
Accrued insurance	**1,344**	(1,029)	(3,703)
Accrual for termite contracts	**(3,000)**	(2,111)	(5,046)
Accrued pension	**(5,000)**	(5,000)	(3,000)
Long-term accrued liabilities	**(5,219)**	(1,169)	(5,525)
Net cash provided by operating activities	**85,201**	76,750	71,513
INVESTING ACTIVITIES			
Purchase of equipment and property	**(18,729)**	(25,541)	(14,204)
Acquisitions of companies	**(10,087)**	(27,239)	(98,090)
Sales/(purchases) of marketable securities, net			21,866
Cash from Sales of Franchises	**707**	639	414
Proceeds from sales of assets	**128**	754	25,726
Net cash used in investing activities	**(27,981)**	(51,387)	(64,288)
FINANCING ACTIVITIES			
Dividends paid	**(17,025)**	(13,714)	(10,924)
Common stock purchased	**(19,452)**	(30,308)	(937)
Common stock options exercised	**1,086**	3,315	2,015
Principal Payments on Capital Lease Obligations	**(763)**		
Other	**(235)**	558	(590)
Net cash used in financing activities	**(36,389)**	(40,149)	(10,436)
Effect of exchange rate changes on cash	**(552)**	1,114	408
Net increase/(decrease) in cash and cash equivalents	**20,279**	(13,672)	(2,803)
Cash and cash equivalents at beginning of year	**43,065**	56,737	59,540
Cash and cash equivalents at end of year	**$ 63,344**	$ 43,065	$ 56,737

Supplemental disclosure of cash flow information						
Cash paid for interest	**$**	**57**	$	162	$	257
Cash paid for income taxes	**$**	**31,258**	$	30,084	$	29,011

The accompanying notes are an integral part of these consolidated financial statements

Supplemental Disclosures of Non-Cash Items

Pension Non-cash (increases) decreases in the minimum pension liability which were (charged) credited to other comprehensive income/(loss) were $9.7 million $(13.8) million, and $(32.1) million in 2006, 2005, and 2004, respectively.

Significant Acquisition During 2004 the Company purchased all of the assets and assumed certain liabilities of Western Pest Services ("Western"). The fair values of Western's assets and liabilities at the date of acquisition are presented below:

Real Estate	$	11,170
Customer Contracts		49,300
Trade Name		5,700
Patents		130
Non Compete Agreement		400
Goodwill		35,106
		101,806
Net Liabilities Assumed		8,357
Net Purchase Price	$	110,163

The accompanying notes are an integral part of these consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Years ended December 31, 2006, 2005, and 2004, Rollins, Inc. and Subsidiaries

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Business Description Rollins, Inc. (the "Company") is a national service company with headquarters located in Atlanta, Georgia, providing pest and termite control services to both residential and commercial customers.

Orkin, Inc. ("Orkin"), a wholly owned subsidiary of the Company founded in 1901, is one of the world's largest pest and termite control companies. It provides customized services from over 400 locations to approximately 1.7 million customers. Orkin serves customers in the United States, Canada, Mexico, Panama and Costa Rica, providing essential pest control services and protection against termite damage, rodents and insects to homes and businesses, including hotels, food service establishments, food manufacturers, retailers and transportation companies. Orkin operates under the Orkin® and PCO Services, Inc.® trademarks and the Acurid℠ service mark.

On April 30, 2004, the Company acquired substantially all of the assets and assumed certain liabilities of Western Pest Services ("Western"), and the Company's consolidated financial statements include the operating results of Western from the date of the acquisition.

On October 1, 2005, the Company acquired substantially all of the assets and assumed certain liabilities of the Industrial Fumigant Company ("IFC"), and the Company's consolidated financial statements include the operating results of IFC from the date of the acquisition.

The Company has only one reportable segment, its pest and termite control business. The Company's results of operations and its financial condition are not reliant upon any single customer or a few customers or the Company's foreign operations.

Principles of Consolidation The Company's policy is to consolidate all subsidiaries, investees or other entities where it has voting control, is subject to a majority of the risk of loss or is entitled to receive a majority of residual returns. The Company does not have any subsidiaries or investees where it has less

than a 100% equity interest or less than 100% voting control, nor does it have any interest in other investees, joint ventures, or other entities that require consolidation.

The consolidated financial statements include the accounts of the Company and subsidiaries owned by the Company. All material intercompany accounts and transactions have been eliminated.

Estimates Used in the Preparation of Consolidated Financial Statements The preparation of the consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the accompanying notes and financial statements. Actual results could differ from those estimates.

Revenues The Company's revenue recognition policies are designed to recognize revenues at the time services are performed. For certain revenue types, because of the timing of billing and the receipt of cash versus the timing of performing services, certain accounting estimates are utilized. Residential and commercial pest control services are primarily recurring in nature on a monthly or bi-monthly basis, while certain types of commercial customers may receive multiple treatments within a given month. In general, pest control customers sign an initial one-year contract, and revenues are recognized at the time services are performed. For pest control customers, the Company offers a discount for those customers who prepay for a full year of services. The Company defers recognition of these advance payments and recognizes the revenue as the services are rendered. The Company classifies the discounts related to the advance payments as a reduction in revenues. Termite baiting revenues are recognized based on the delivery of the individual units of accounting. At the inception of a new baiting services contract upon quality control review of the installation, the Company recognizes revenue for the delivery of the monitoring stations, initial directed liquid termiticide treatment and installation of the monitoring services. The amount deferred is the fair value of monitoring services to be rendered after the initial service. The amount deferred for the undelivered monitoring element is then recognized as income on a straight-line basis over the remaining contract term, which results in recognition of revenue in a pattern that approximates the timing of performing monitoring visits. Baiting renewal revenue is deferred and recognized over the annual contract period on a straight-line basis that approximates the timing of performing the required monitoring visits.

Prior to 2004, traditional termite treatments were recognized as revenue at the renewal date and an accrual was established for estimated costs of reapplications and repairs to be incurred. Under the accounting method adopted in 2004, the revenue received is deferred and recognized on a straight-line basis over the remaining contract term; and, the cost of reinspections, reapplications and repairs and associated labor and chemicals are expensed as incurred. For outstanding claims, an estimate is made of the costs to be incurred (including legal costs) based upon current factors and historical information. The performance of reinspections tends to be close to the contract renewal date and, while reapplications and repairs involve an insubstantial number of the contracts, these costs are incurred over the contract term. The accounting principle adopted in 2004 eliminates the need to obtain actuarial estimates of the claim costs to be incurred and management's estimates of reapplication costs. Also, management believes the newly adopted this accounting method more closely conforms to the current pattern under which revenues are earned and expenses are incurred, and conforms to the accounting methodology of Orkin and its subsidiary, Western Pest Services. The costs of providing termite services upon renewal are compared to the expected revenue to be received and a provision is made for any expected losses.

Due to this change, in 2004 the Company recorded a cumulative adjustment to reduce net income by $6.2 million (net of income taxes). As the revenue is being deferred, the future cost of reinspections, reapplications and repairs and associated labor and chemicals applicable to the deferred revenue are expensed as incurred and no longer accrued. The Company will continue to accrue for noticed claims.

The Company's foreign operations accounted for approximately 7% of total revenues for the years ended December 31, 2006, 2005 and 2004. Revenues are presented net of sales taxes.

Interest income on installment receivables is accrued monthly based on actual loan balances and stated interest rates. Franchise fees are treated as unearned revenue in the Statement of Financial Position for the duration of the initial contract period. Royalties from Orkin franchises are accrued and recognized as revenues as earned on a monthly basis. Gains on sales of pest control customer accounts to franchises are recognized at the time of sale and when collection is reasonably assured.

Allowance for Doubtful Accounts The Company maintains an allowance for doubtful accounts based on the expected collectibility of accounts receivable. Management uses historical collection results as well as accounts receivable aging in order to determine the expected collectibility of accounts receivable.

Advertising Advertising expenses are charged to expense during the year in which they are incurred. The total advertising costs were approximately $36.0 million, $34.1 million, and $33.4 million 2006, 2005, and 2004, respectively.

Cash and Cash Equivalents The Company considers all investments with an original maturity of three months or less to be cash equivalents. Short-term investments, included in cash and cash equivalents, are stated at cost, which approximates fair market value. As of December 31, 2006 and 2005, cash held in foreign bank accounts amounted to approximately $9.5 million and $6.2 million, respectively.

Marketable Securities From time to time, the Company maintains investments held by several large, well-capitalized financial institutions. The Company's investment policy does not allow investment in any securities rated less than "investment grade" by national rating services. The Company's marketable securities generally consist of United States government, corporate and municipal debt securities.

Management determines the appropriate classification of debt securities at the time of purchase and re-evaluates such designations as of each balance sheet date. Debt securities are classified as available-for-sale because the Company does not have the intent to hold the securities to maturity. Available-for-sale securities are stated at their fair values, with the unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity. Realized gains and losses and declines in value judged to be other than temporary on available-for-sale securities are included in interest income.

Materials and Supplies Materials and supplies are recorded at the lower of cost (first-in, first-out basis) or market.

Income Taxes The Company provides for income taxes based on Statement of Financial Accounting Standards (SFAS) No. 109, *Accounting for Income Taxes*, which requires recognition of deferred tax liabilities and assets for the expected future tax consequences of events that have been included in the consolidated financial statements or tax returns. The Company provides an allowance for deferred tax assets when it is determined that it is more likely than not that the deferred tax assets will not be utilized.

Equipment and Property Depreciation and amortization, which includes the amortization of assets recorded under capital leases, are provided principally on a straight-line basis over the estimated useful lives of the related assets. Annual provisions for depreciation of $13.0 million in 2006, $11.5 million in 2005, $12.1 and million in 2004 have been reflected in the Consolidated Statements of Income in the line item entitled Depreciation and Amortization. These annual provisions for depreciation are computed using the following asset lives: buildings, ten to forty years; and furniture, fixtures, and operating equipment, three to ten years. Expenditures for additions, major renewals and betterments are capitalized and expenditures for maintenance and repairs are expensed as incurred. The cost of assets retired or otherwise disposed of and the related accumulated depreciation and amortization are eliminated from the accounts in the year of disposal with the resulting gain or loss credited or charged to income.

Goodwill and Other Intangible Assets In accordance with SFAS No. 142, "*Goodwill and Other Intangible Assets"*, the Company classifies intangible assets into three categories: (1) intangible assets with definite lives subject to amortization; (2) intangible assets with indefinite lives not subject to amortization; and

(3) goodwill. The Company does not amortize intangible assets with indefinite lives or goodwill. Goodwill and other intangible assets with indefinite useful lives are tested for impairment annually or more frequently if events or circumstances indicate the assets might be impaired. Such conditions may include an economic downturn or a change in the assessment of future operations. The Company performs impairment tests of goodwill at the company level. Such impairment tests for goodwill include comparing the fair value of the appropriate reporting unit (the Company) with its carrying value. The Company performs impairment tests for indefinite-lived intangible assets by comparing the fair value of each indefinite-lived intangible asset unit to its carrying value. The Company recognizes an impairment charge if the asset's carrying value exceeds its estimated fair value. The Company completed its annual impairment analyses as of September 30, 2006. Based upon the results of these analyses, the Company has concluded that no impairment of its goodwill or other intangible assets was indicated.

Impairment of Long-Lived Assets) In accordance with SFAS 144, "*Accounting for the Impairment or Disposal of Long-Lived Assets"*, the Company's long-lived assets, such as property and equipment and intangible assets with definite lives are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated undiscounted future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset. Based upon the results of these analyses, the Company has concluded that no impairment of its long-lived assets was indicated.

Insurance The Company self-insures, up to specified limits, certain risks related to general liability, workers' compensation and vehicle liability. The estimated costs of existing and future claims under the self-insurance program are accrued based upon historical trends as incidents occur, whether reported or unreported (although actual settlement of the claims may not be made until future periods) and may be subsequently revised based on developments relating to such claims. The Company contracts an independent third party actuary on an annual basis to provide the Company an estimated liability based upon historical claims information. The actuarial study is a major consideration, along with management's knowledge of changes in business practice and existing claims compared to current balances. The reserve is established based on all these factors. Management's judgment is inherently subjective and a number of factors are outside management's knowledge and control. Additionally, historical information is not always an accurate indication of future events.

Accrual for Termite Contracts The Company maintains an accrual for termite claims representing the estimated costs of reapplications, repairs and associated labor and chemicals, settlements, awards and other costs relative to termite control services. Factors that may impact future cost include termiticide life expectancy and government regulation. It is significant that the actual number of claims has decreased in recent years due to changes in the Company's business practices. However, it is not possible to precisely predict future significant claims. Positive changes to our business practices include revisions made to our contracts, more effective treatment methods that include a directed-liquid and baiting program, more effective termiticides and expanded training.

Contingency Accruals The Company is a party to legal proceedings with respect to matters in the ordinary course of business. In accordance with Statement of Financial Accounting Standards No. 5, *Accounting for Contingencies,* the Company estimates and accrues for its liability and costs associated with the litigation. Estimates and accruals are determined in consultation with outside counsel. It is not possible to accurately predict the ultimate result of the litigation. However, in the opinion of management, the outcome of the litigation will not have a material adverse impact on the Company's financial condition or results of operations.

Treasury Shares The Company records treasury stock repurchases at par value and records the difference between cost and par value as a reduction of treasury stock additional paid-in-capital and retained

earnings. During 2006, 1.0 million shares were repurchased for $19.4 million. During 2005, 1.7 million shares were repurchased for $30.2 million. During 2004, 57 thousand shares were repurchased for $900 thousand.

Earnings Per Share In accordance with SFAS No. 128, *Earnings Per Share* ("EPS"), the Company presents basic EPS and diluted EPS. Basic EPS is computed on the basis of weighted-average shares outstanding. Diluted EPS is computed on the basis of weighted-average shares outstanding plus common stock options outstanding during the year, which, if exercised, would have a dilutive effect on EPS. Prior basic and diluted EPS for all years has been restated for the stock split effective March 10, 2005. A reconciliation of the number of weighted-average shares used in computing basic and diluted EPS is as follows:

	Years ended December 31,		
(in thousands, except per share data)	**2006**	**2005**	**2004**
Basic and diluted earnings available to stockholders (numerator):	**$ 57,809**	$ 52,773	$ 52,055
Shares (denominator):			
Weighted-average shares outstanding Basic	**67,165**	67,898	68,321
Effect of dilutive securities:			
Employee Stock Options	**1,711**	1,874	1,846
Weighted-average shares outstanding Diluted	**68,876**	69,772	70,167
Per share amounts:			
Basic income per common share	**$ 0.86**	$ 0.78	$ 0.76
Diluted income per common share	**$ 0.84**	$ 0.76	$ 0.74

Translation of Foreign Currencies Assets and liabilities reported in functional currencies other than U.S. dollars are translated into U.S. dollars at the year-end rate of exchange. Revenues and expenses are translated at the weighted-average exchange rates for the year. The resulting translation adjustments are charged or credited to other comprehensive income. Gains or losses from foreign currency transactions, such as those resulting from the settlement of receivables or payables, denominated in foreign currency are included in the earnings of the current period.

Stock-Based Compensation The Company adopted FAS 123R as of January 1, 2006. Through December 31, 2005, the Company has followed APB 25 to account for employee stock options. Under APB 25, the intrinsic value method of accounting, no compensation expense is recognized because the exercise price of the employee stock options equals the market price of the underlying stock on the date of grant. The Company applied FAS 123 for disclosure purposes only, and recognized compensation expense on a straight-line basis over the vesting period of the award.

In order to estimate the fair value of stock options, the Company used the Black-Scholes option valuation model, which was developed for use in estimating the fair value of publicly traded options which have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions and these assumptions can vary over time.

The following proforma net income and earnings per share (or "EPS") for 2004 and 2005 were determined as if the Company had accounted for employee stock options and stock issued under its employee stock

plans using the fair value method prescribed by FAS 123. The 2006 actuals are presented for comparative purposes only.

	Years ended December 31,		
(in thousands, except per share data)	**2006 as reported**	**2005 pro-forma**	**2004 pro-forma**
Net income, as reported	**$ 57,809**	$ 52,773	$ 52,055
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects		(684)	(801)
Pro forma net income	**$ 57,809**	$ 52,089	$ 51,254
Income per share:			
Basic as reported	**$ 0.86**	$ 0.78	$ 0.76
Basic pro forma		$ 0.77	$ 0.75
Diluted as reported	**$ 0.84**	$ 0.76	$ 0.74
Diluted pro forma		$ 0.75	$ 0.73

The Company did not grant any stock options during 2006, 2005 or 2004.

Comprehensive Income (Loss) Other Comprehensive Income (Loss) results from foreign currency translations, minimum pension liability adjustments, and unrealized loss on marketable securities.

Franchising Program Orkin had 58 franchises as of December 31, 2006, including international franchises in Mexico, established in 2000, Panama, established in 2003, and Costa Rica, established in 2006. Transactions with franchises involve sales of customer contracts to establish new franchises, initial franchise fees and royalties. The customer contracts and initial franchise fees are typically sold for a combination of cash and notes due over periods ranging up to 5 years. Notes receivable from franchises aggregated $5.2 million, $5.5 million, and $5.2 million as of December 31, 2006, December 31, 2005, and December 31, 2004, respectively. The Company recognizes gains from the sale of customer contracts at the time they are sold to franchises and collection on the notes is reasonably assured. The Company recognized overall gain for the sale of customer contracts of $1.0 million for the year ended December 31, 2006 compared to $1.5 million for the year ended December 31, 2005 and $1.7 million for the year ended December 31, 2004, and these amounts are included as revenues in the accompanying Consolidated Statements of Income. Initial franchise fees are deferred for the duration of the initial contract period and are included as unearned revenue in the Consolidated Statements of Financial Position. Deferred franchise fees amounted to $2.2 million, $2.0 million, and $1.6 million at December 31, 2006, December 31, 2005, and December 31, 2004, respectively. Royalties from franchises are accrued and recognized as revenues as earned on a monthly basis. Revenues from royalties were $2.2 million for the year ended December 31, 2006 compared to $2.0 million for the year ended December 31, 2005 and $1.7 million for the year ended December 31, 2004. The Company's maximum exposure to loss relating to the franchises aggregated $3.0 million, $3.5 million, and $3.6 million at December 31, 2006, December 31, 2005 and December 31, 2004, respectively.

Fair Value of Financial Instruments The Company's financial instruments consist of cash and cash equivalents, short-term investments, marketable securities, trade and notes receivables, accounts payable and other short-term liabilities. The carrying amounts of these financial instruments approximate their fair values.

Three-for-Two Stock Split The Board of Directors, at its quarterly meeting on January 25, 2005, authorized a three-for-two stock split by the issuance on March 10, 2005 of one additional common share for each two common shares held of record at February 10, 2005. Accordingly, the par value for additional shares issued was adjusted to common stock, and fractional shares resulting from the stock split were settled in cash. All share and per share data appearing in the consolidated financial statements and related notes have been retroactively adjusted for this split.

Cumulative Effect of Change in Accounting Principle Prior to 2004, traditional termite treatments were recognized as revenue at the renewal date and an accrual was established for estimated costs of reapplications and repairs to be incurred. Beginning fourth quarter 2004, the Company adopted an accounting method under which the revenue received is deferred and recognized on a straight-line basis over the remaining contract term; and, the cost of reinspections, reapplications and repairs and associated labor and chemicals are expensed as incurred and no longer accrued. For noticed claims, an estimate is made of the costs to be incurred (including legal costs) based upon current factors and historical information. The performance of reinspections tends to be close to the contract renewal date and, while reapplications and repairs involve an insubstantial number of the contracts, these costs are incurred over the contract term. The accounting principle adopted in 2004 eliminates the need to obtain actuarial estimates of the claim costs to be incurred and management's estimates of reapplication costs. Also, management believes the newly adopted accounting method more closely conforms to the current pattern under which revenues are earned and expenses are incurred, and conforms the accounting methodology of Orkin and its recently acquired subsidiary, Western Pest Services. The costs of providing termite services upon renewal are compared to the expected revenue to be received and a provision is made for any expected losses.

Due to this change, the Company recorded a cumulative effect adjustment to reduce net income by $6.2 million (net of income taxes) during 2004.

New Accounting Standards

Recently Adopted Accounting Pronouncements

Statements of Financial Accounting Standards

In January 2006, the Company adopted *SFAS No. 123, "Share-Based Payment (Revised 2004)."* SFAS 123R establishes standards for the accounting for transactions in which an entity (i) exchanges its equity instruments for goods or services, or (ii) incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of the equity instruments. SFAS 123R eliminates the ability to account for stock-based compensation using APB 25 and requires that such transactions be recognized as compensation cost in the income statement based on their fair values on the measurement date, which is generally the date of the grant. The Company adopted the provisions of SFAS 123R on January 1, 2006. Details related to the adoption of SFAS 123R and the impact to the Company's financial statements are more fully discussed in Note 8 Employee Benefit and Stock Compensation Plans.

In September 2006, the FASB issued *SFAS No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88 106, and 132(R)."* SFAS 158 requires an employer to recognize the overfunded or underfunded status of defined benefit post-retirement plans as an asset or a liability in its statement of financial position. The funded status is measured as the difference between plan assets at fair value and the benefit obligation (the projected benefit obligation for pension plans or the accumulated benefit obligation for other post-retirement benefit plans). An employer is also required to measure the funded status of a plan as of the date of its year-end statement of financial position with changes in the funded status recognized through comprehensive income. SFAS 158 also requires certain disclosures regarding the effects on net periodic benefit cost for the next fiscal year that arise from delayed recognition of gains or losses, prior service costs or credits, and the transition asset or obligation. The Company was required to recognize the funded status of the plan in its financial statements for the year ended December 31, 2006. The Company had previously recognized the funded status of the plan in prior financial statements. See Note 8 Employee Benefit and Stock Compensation Plans for additional information related to this plans. The requirement to measure plan assets and benefit obligations as of the date of the year-end statement of financial position is effective

for the Company's financial statements beginning with the year ended after December 15, 2008. The Company currently uses December 31 as the measurement date for the plans.

SEC Staff Accounting Bulletins

In September 2006, the SEC issued *Staff Accounting Bulletin (SAB) No. 108, "Considering the Effects of a Prior Year Misstatements When Quantifying Misstatements in Current Year Financial Statements."* SAB 108 addresses how the effects of prior year uncorrected errors must be considered in quantifying misstatements in the current year financial statements. The effects of prior year uncorrected errors include the potential accumulation of improper amounts that may result in a material misstatement on the balance sheet or the reversal of prior period errors in the current period that result in a material misstatement of the current period income statement amounts. Adjustments to current or prior period financial statements would be required in the event that after application of various approaches for assessing materiality of a misstatement in current period financial statements and consideration of all relevant quantitative and qualitative factors, a misstatement is determined to be material. SAB 108 is applicable to all financial statements issued by the Company after November 15, 2006. SAB 108 became affective for the Company's fiscal year ended December 31, 2006 and did not have a material effect on our financial position or results of operations for the year ended December 31, 2006.

Recently Issued Accounting Pronouncements

Statements of Financial Accounting Standards

In September 2006, the FASB issued *SFAS No. 157, "Fair Value Measurements."* SFAS 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS 157 is effective for the Company on January 1, 2008 and is not expected to have a significant impact on the Company's financial statements.

Financial Accounting Standards Board Staff Positions and Interpretations

In July 2006, the FASB issued Interpretation No. 48 (FIN 48), "Accounting for Uncertainty in Income Taxes an Interpretation of SFAS No. 109." FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes." FIN 48 prescribes a recognition threshold and measurement of a tax position taken or expected to be taken in an enterprise's tax return. In addition, FIN 48 provides guidance on derecognition, classification, interest, penalties, accounting in interim periods and disclosure related to uncertain income tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006. Accordingly, the Company will be required to adopt FIN 48 in first quarter 2007. The Company is currently evaluating the impact that the adoption of FIN 48 will have, if any, on its consolidated financial statements and notes thereto.

2. TRADE RECEIVABLES

Trade receivables, net, at December 31, 2006, totaling $61.5 million and at December 31, 2005, totaling $57.1 million, are net of allowances for doubtful accounts of $7.2 million and $5.6 million, respectively. Trade receivables include installment receivable amounts, which are due subsequent to one year from the balance sheet dates. These amounts were approximately $8.8 million and $9.4 million at the end of 2006 and 2005, respectively. Trade receivables also include note receivables due from franchises, which amounted to $5.2 million and $5.5 million as of December 31, 2006 and 2005, respectively. The carrying amount of notes receivable approximates fair value as the interest rates approximate market rates for these types of contracts. The Allowance For Doubtful Accounts is principally calculated based on the application of estimated loss percentages to delinquency aging totals, based on contractual terms, for the various categories of receivables. Bad debt write-offs occur according to company policies that are specific to pest

control, commercial and termite accounts. At any given time, the Company may have immaterial amounts due from related parties, which are invoiced and settled on a regular basis. Receivables due from related parties were approximately $115,000 as of December 31, 2006, and approximately $82,000 as of December 31, 2005.

3. EQUIPMENT AND PROPERTY

Equipment and property are presented at cost less accumulated depreciation and are detailed as follows:

	December 31,	
(in thousands)	**2006**	**2005**
Buildings	**$ 30,367**	$ 25,788
Operating Equipment	**55,291**	47,787
Furniture and Fixtures	**8,058**	6,863
Computer Equipment and Systems	**35,536**	31,423
	129,252	111,861
Less Accumulated Depreciation	**77,868**	67,037
	51,384	44,824
Land	**20,757**	21,108
Net property, plant and equipment	**$ 72,141**	$ 65,932

4. GOODWILL AND OTHER INTANGIBLE ASSETS

Intangibles consist primarily of goodwill and customer contracts and also include trademarks and non-compete agreements, all related to businesses acquired. Goodwill represents the excess of the purchase price over the fair value of net assets of businesses acquired. The carrying amount of goodwill and certain indefinite lived trademarks was $133.6 million as of December 31, 2006 and $133.7 million as of December 31, 2005.

On January 1, 2002, the Company adopted FASB Statement No. 142, *Goodwill and Other Intangible Assets*. As of January 1, 2002, amortization of goodwill and trademarks was terminated, and instead the assets are subject to periodic testing for impairment. The Company completed its annual impairment analyses as of September 30, 2006. Based upon the results of these analyses, the Company has concluded that no impairment of its goodwill or trademarks has occurred.

Customer contracts and non-compete agreements are amortized on a straight-line basis over the period of the agreements, as straight-line best approximates the ratio that current revenues bear to the total of current and anticipated revenues, based on the estimated lives of the assets. In accordance with Statement 142, the expected lives of customer contracts and non-compete agreements were reviewed, and it was determined that customer contracts should be amortized over a life of 8 to 12 1/2 years dependent upon customer type. The carrying amount and accumulated amortization for customer contracts and non-competes were as follows:

	December 31,	
(in thousands)	**2006**	**2005**
Customer contracts and non-competes	**$ 127,018**	$ 118,746
Less: Accumulated amortization	**(58,408)**	(46,905)
Customer contracts and non-competes, net	**$ 68,610**	$ 71,841

Total intangible amortization expense was approximately $13.9 million in 2006, $12.8 million in 2005 and $10.9 million in 2004. Estimated amortization expense for each of the five succeeding fiscal years is as follows:

(in thousands)	
2006	$ 13,146
2007	$ 12,027
2008	$ 10,560
2009	$ 9,131
2010	$ 8,961

5. INCOME TAXES

The Company's income tax provision consisted of the following:

	December 31,		
(in thousands)	2006	2005	2004
Current:			
Federal	**$ 27,537**	$ 26,973	$ 22,704
State	**2,579**	2,998	3,109
Foreign	**1,227**	1,558	1,562
Deferred:			
Federal	**2,864**	1,146	10,459
State	**2,984**	2,239	3,026
Foreign	**159**	268	(407)
Total income tax provision	**$ 37,350**	$ 35,182	$ 40,453

The primary factors causing income tax expense to be different than the federal statutory rate for 2006, 2005 and 2004 are as follows:

	December 31,		
(in thousands)	2006	2005	2004
Income tax at statutory rate	**$ 33,306**	$ 30,784	$ 34,548
State income tax expense (net of federal benefit)	**3,161**	3,404	3,986
Foreign tax expense	**446**	800	726
Other	**437**	194	1,193
Total income tax provision	**$ 37,350**	$ 35,182	$ 40,453

The Provision for Income Taxes resulted in an effective tax rate of 39.25% on Income Before Income Taxes for the year ended December 31, 2006. For 2005 the effective tax rate was 40.0% and for 2004 the effective tax rate was 41.0%. The effective income tax rate differs from the annual federal statutory tax rate primarily because of state and foreign income taxes. During 2006, 2005 and 2004, the Company paid income taxes of $31.3 million, $30.1 million and $29.0 million, respectively, net of refunds.

Deferred income taxes reflect the net tax effects of the temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and income tax purposes. Significant

components of the Company's deferred tax assets and liabilities at December 31, 2006 and 2005 are as follows:

	December 31,	
(in thousands)	**2006**	**2005**
Deferred Tax Assets:		
Termite Accrual	**$ 6,611**	$ 7,963
Insurance and Contingencies	**15,853**	18,900
Unearned Revenue	**11,258**	12,760
Compensation Benefits	**3,434**	2,798
Net Pension Liability	**2,799**	8,116
State Operating Loss Carryforwards	**10,197**	10,017
Other	**4,827**	4,148
Valuation Allowance	**(8,563)**	(6,279)
Total Deferred Tax Assets	**46,416**	58,423
Deferred Tax Liabilities		
Depreciation and Amortization	**(10,049)**	(12,143)
Foreign Currency Translation	**(1,922)**	(1,516)
Other	**(940)**	(1,307)
Total Deferred Tax Liabilities	**(12,911)**	(14,966)
Net Deferred Tax Assets	**33,505**	**43,457**

Analysis of the valuation allowance

	December 31,	
(in thousands)	**2006**	**2005**
Valuation allowance at beginning of year	**$ 6,279**	$ 6,287
Increase (decrease) in valuation allowance	**2,284**	(8)
Valuation allowance at end of year	**$ 8,563**	$ 6,279

As of December 31, 2006, the Company has net operating loss carryforwards for state income tax purposes of approximately $257 million, which will be available to offset future state taxable income. If not used, these carryforwards will expire between 2008 and 2024. The state net operating losses and the valuation allowance are presented on a gross basis for 2006 and 2005. Management believes that it is unlikely to be able to utilize approximately $220 million of these net operating losses before they expire and has included a valuation allowance for the effect of these unrealizable operating loss carryforwards. The valuation allowance increased by $2.3 million due to additional losses generated in the current year.

The Company is currently under audit by the Internal Revenue Service (IRS) for tax years 2002 and 2003. The IRS has issued Notices of Proposed Adjustment with respect to various issues. The Company has reviewed its position regarding the adjustments and plans to defend against those adjustments that are without merit. The Company does not expect the resolution of these issues, taken individually or in the aggregate, to have a material adverse impact on the Company's financial condition or results of operations.

Earnings from continuing operations before income tax includes foreign income of $2.7 million in 2006, $2.2 million in 2005 and $2.4 million in 2004. The Company intends to reinvest indefinitely the undistributed earnings of some of its non-U.S. subsidiaries. As of December 31, 2006, the Company had approximately $5.4 million of earnings from those international subsidiaries that had not been remitted to the United States. Should these earnings be distributed in the form of dividends or alternative means, the

distribution would be subject to U.S. federal income tax at the statutory rate of 35 percent, less foreign tax credits applicable to such distributions.

6. ACCRUAL FOR TERMITE CONTRACTS

In accordance with SFAS No. 5, *"Accounting for Contingencies,"* the Company maintains an accrual for termite claims representing the estimated costs of reapplications, repairs and associated labor and chemicals, settlements, awards and other costs relative to termite control services. Factors that may impact future cost include termiticide life expectancy and government regulation.

A reconciliation of changes in the accrual for termite contracts for the years ended December 31, 2006, 2005 and 2004 is as follows:

	December 31,		
(in thousands)	**2006**	**2005**	**2004**
Beginning balance	**$ 23,200**	$ 25,311	$ 43,873
Effect of change in accounting principle			(15,309)
Western Pest Services opening entry			372
Current year provision	**14,420**	16,679	13,433
Settlements, claims, and expenditures	**(17,419)**	(18,790)	(17,058)
Ending balance	**$ 20,201**	$ 23,200	$ 25,311

7. COMMITMENTS AND CONTINGENCIES

The Company leases vehicles and equipment under operating and capital leases which are accounted for accordingly. The capital leases contractually expire at various dates through 2008. The assets and liabilities acquired under capital leases are recorded at the lower of fair market value or the present value of future lease payments, and are depreciated over the actual contract term. Depreciation of assets under capital leases is included in depreciation expense for 2006 and 2005.

Following is a summary of property held under capital leases:

(in thousands)	**2006**	**2005**
Vehicles	**$ 1,428**	$ 2,234
Extensions	**7**	
Accumulated Depreciation	**(819)**	(871)
Total property held under capital leases	**$ 616**	$ 1,363

The remainder of the leases is accounted for as operating leases expiring at various dates through 2017. Rental expense under operating lease obligations was $34.9 million, $34.9 million and $30.3 million for the years ended December 31, 2006, 2005 and 2004, respectively.

Future commitments under operating and capital leases are as summarized:

(in thousands)	Operating leases	Capital leases
2007	$ 22,428	$ 498
2008	18,236	113
2009	10,540	11
2010	7,115	
2011	4,455	
Thereafter	6,280	
Total minimum obligation	$ 69,054	$ 622
Interest component of obligation		(6)
Present value of minimum obligation	$ 69,054	$ 616

The Company maintains credit facilities with two banks that allow it to borrow up to $70.0 million on an unsecured basis at the bank's prime rate of interest or the indexed London Interbank Offered Rate (LIBOR) under which $38.8 million in Letters of Credit were outstanding at December 31, 2006. No borrowings were outstanding under this credit facility as of December 31, 2006, 2005 or 2004.

Orkin, one of the Company's subsidiaries, is a named defendant in Mark and Christine Butland et al. v. Orkin Exterminating Company, Inc. et al. pending in the Circuit Court of Hillsborough County, Tampa, Florida. The plaintiffs filed suit in March of 1999 and are seeking monetary damages and injunctive relief. The Court ruled in early April 2002, certifying the class action lawsuit against Orkin. Orkin appealed this ruling to the Florida Second District Court of Appeals, which remanded the case back to the trial court for further findings. In December 2004 the Court issued a new ruling certifying the class action. Orkin appealed this new ruling to the Florida Second District Court of Appeals. In June 2006, the Florida Second District Court of Appeals issued a ruling denying certification of the class. Following the Plaintiffs' motion for rehearing, the court upheld its prior decision that class certification was improper but also ruled that the Plaintiffs can return to the trial court and attempt to certify a narrower class. Orkin will vigorously oppose any effort by the Plaintiffs to do so. Orkin believes this case to be without merit and intends to defend itself vigorously through trial, if necessary. At this time, the final outcome of the litigation cannot be determined. However, in the opinion of management, the ultimate resolution of this action will not have a material adverse effect on the Company's financial position, results of operations or liquidity.

Additionally, in the normal course of business, Orkin is a defendant in a number of lawsuits, which allege that plaintiffs have been damaged as a result of the rendering of services by Orkin. Orkin is actively contesting these actions. Some lawsuits or arbitrations have been filed (Ernest W. Warren and Dolores G. Warren et al. v. Orkin Exterminating Company, Inc., et al.; and Francis D. Petsch, et al. v. Orkin Exterminating Company, Inc. et al.) in which the Plaintiffs are seeking certification of a class. The cases originate in Georgia and Florida. In Warren, the Superior Court of Cobb County, Marietta, Georgia, ruled in August 2006, certifying the class action against Orkin. Orkin has appealed this ruling to the Georgia Court of Appeals. The Company believes these matters to be without merit and intends to vigorously contest certification and defend itself through trial or arbitration, if necessary. In the opinion of management, the outcome of these actions will not have a material adverse effect on the Company's financial position, results of operations or liquidity.

Orkin is involved in certain environmental matters primarily arising in the normal course of business. In the opinion of management, the Company's liability under any of these matters would not materially affect its financial condition or results of operations. Consistent with the Company's responsibilities under various regulations, the Company undertakes environmental assessments and remediation of hazardous substances from time to time as the Company determines its responsibilities for these purposes. As these situations arise, the Company accrues management's best estimate of future costs for these activities.

Based on management's current estimates of these costs, management does not believe these costs are material to the Company's financial condition or operating results.

8. EMPLOYEE BENEFIT AND STOCK COMPENSATION PLANS

The Company maintains a noncontributory tax-qualified defined benefit retirement plan (the "Plan") covering employees meeting certain age and service requirements. The Plan provides benefits based on the average compensation for the highest five years during the last ten years of credited service (as defined) in which compensation was received, and the average anticipated Social Security covered earnings. The Company funds the Plan with at least the minimum amount required by ERISA. The Company made contributions of $5.0 million to the plan during the year ended December 31, 2006, $5.0 million during the year ended December 31, 2005 and $3.0 million during the year ended December 31, 2004. Effective January 1, 2002, the Company adopted amendments to the Plan including a change to the benefit calculation and limiting plan participation to current participants. These amendments are reflected in benefit obligations below.

In June 2005, the Company recorded a $4.2 million non-cash curtailment gain in accordance with SFAS No. 88, "Employer's Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits", ("SFAS No. 88") in connection with freezing our defined benefit pension plan, using actuarial assumptions consistent with those used at December 31, 2004. SFAS No. 88 requires curtailment accounting if an event eliminates, for a significant number of employees, the accrual of defined benefits for some or all of their future services. In the event of a curtailment, an adjustment must be recognized for the unrecognized prior service cost associated with years of service no longer expected to be rendered.

The Company currently uses December 31 as the measurement date for its defined benefit post-retirement plans. The funded status of the Plan and the net amount recognized in the statement of financial position are summarized as follows as of December 31:

	December 31,	
(in thousands)	**2006**	**2005**
Accumulated Benefit Obligation, end of year	**$ 153,598**	$ 153,027
CHANGE IN BENEFIT OBLIGATION		
Benefit obligation at beginning of year	**$ 153,027**	$ 148,921
Service Cost		2,794
Interest Cost	**8,139**	8,367
Curtailment		(15,251)
Actuarial (gain) loss	**(2,562)**	12,855
Benefits Paid	**(5,006)**	(4,659)
Obligation at End of Year	**$ 153,598**	$ 153,027
CHANGE IN PLAN ASSETS		
Market Value of Plan Assets at Beginning of Year	**$ 132,376**	$ 123,712
Actual Return on Plan Assets	**14,282**	8,323
Employer Contribution	**5,000**	5,000
Benefits Paid	**(5,006)**	(4,659)
Fair Value of Plan Assets at End of Year	**$ 146,652**	$ 132,376
Funded Status	**(6,946)**	(20,651)
Unrecognized Net Actuarial Loss		45,957
Unrecognized Prior Service Benefit		
Net Amount Recognized		$ 25,306

Amounts Recognized in the Statement of Financial Position consist of:

(in thousands)	December 31, 2006
Noncurrent assets	$
Current liabilities	
Noncurrent liabilities	(6,946)
	$ (6,946)

Amounts Recognized in Accumulated Other Comprehensive Income consists of:

(in thousands)	December 31, 2006
Net loss	$ 36,283
Prior service cost	
Net transition obligation	
	$ 36,283

The accumulated benefit obligation for the defined benefit pension plan was $153.6 million and $153.0 million at December 31, 2006 and 2005, respectively. (Increases) decreases in the minimum pension liability which were (charged, net of tax) credited to other comprehensive income (loss) were $9.7 million, ($13.8) million and ($32.1) million in 2006, 2005 and 2004, respectively.

The following weighted-average assumptions as of December 31 were used to determine the projected benefit obligation and net benefit cost:

December 31,	2006	2005
PROJECTED BENEFIT OBLIGATION		
Discount rate	**5.50%**	5.50%
Rate of compensation increase	**N/A**	N/A
NET BENEFIT COST		
Discount rate	**5.50%**	5.75%
Expected return on plan assets	**8.00%**	8.00%

The return on plan assets reflects the weighted-average of the expected long-term rates of return for the broad categories of investments held in the plan. The expected long-term rate of return is adjusted when there are fundamental changes in the expected returns on the plan investments.

The discount rate reflects the current rate at which the pension liabilities could be effectively settled at the end of the year. In estimating this rate, the Company utilizes the Moody's Aa long-term corporate bond yield with a yield adjustment made for the longer duration of the Company's obligations. A lower discount rate increases the present value of benefit obligations

Components of Net Periodic Benefit Cost and Other Amounts Recognized in Other Comprehensive Income

(in thousands)	Pension Benefits 2006	2005	2004
Net Periodic Benefit Cost			
Service cost	**$**	$ 2,794	$ 5,186
Interest cost	**8,139**	8,367	8,298
Expected return on plan assets	**(10,733)**	(9,864)	(9,576)
Amortization of prior service cost		(434)	(868)
Amortization of net loss	**3,563**	4,552	3,379
Net periodic benefit cost	**969**	5,415	6,419
Curtailment Gain		(4,176)	
Net Periodic Benefit Cost After Curtailments and Settlements	**$ 969**	$ 1,239	$ 6,419
Other Changes in Plan Assets and Benefit Obligations Recognized in Other Comprehensive Income			
Net gain	**$ (6,111)**		
Amortization of net loss	**(3,563)**		
Total recognized in other comprehensive income	**(9,674)**		
Total recognized in net periodic benefit cost and other comprehensive income	**$ (8,705)**		

The estimated net loss that will be amortized in 2007 is expected to be $3.7 million. At December 31, 2006 and 2005, the Plan's assets were comprised of listed common stocks and U.S. government and corporate securities. Included in the assets of the Plan were shares of Rollins, Inc. Common Stock with a market value of $15.1 million and $13.4 million at December 31, 2006 and 2005, respectively.

The Plan's weighted average asset allocation at December 31, 2006 and 2005 by asset category, along with the target allocation for 2007, are as follows:

Asset category	Target allocations for 2007	Percentage of plan assets as of December 31, 2006	2005
Equity Securities Rollins stock	**7.9%**	10.3%	10.1%
Equity Securities all other	**44.3%**	44.5%	43.4%
Debt Securities core fixed income	**26.1%**	25.6%	25.8%
Tactical-Fund of Equity & Debt Securities	**4.9%**	4.8%	2.4%
Real Estate	**4.9%**	4.9%	4.8%
Other	**11.9%**	9.9%	13.5%
Total	**100.0%**	100.0%	100.0%

Our investment strategy for our pension plan is to maximize the long-term rate of return on plan assets within an acceptable level of risk in order to minimize the cost of providing pension benefits. The investment policy establishes a target allocation for each asset class, which is rebalanced as required. The plan utilizes a number of investment approaches, including individual market securities, equity and fixed income funds in which

the underlying securities are marketable, and debt funds to achieve this target allocation. The Company expects to contribute approximately $2.5 million to the pension plan in 2007 and

does not expect to receive a refund in 2007. The estimated future benefit payments over the next ten years are as follows:

(in thousands)		
2007		5,421
2008		5,749
2009		6,207
2010		6,660
2011		7,219
Thereafter		44,800
Total estimated benefits payments	$	76,056

The Company sponsors a deferred compensation 401(k) plan that is available to substantially all employees with six months of service. The plan provides for a matching contribution (made in the form of Common Stock of the Company) of fifty cents ($.50) for each one dollar ($1.00) beginning January 1, 2005 and thirty cents ($.30) for each one dollar ($1.00) prior to January 1, 2005 of a participant's contributions to the plan that do not exceed 6 percent of his or her annual compensation (which includes commissions, overtime and bonuses). The charge to expense for the Company match was approximately $4.7 million in 2006, $4.2 million in 2005 and $2.7 million in 2004. At December 31, 2006, 2005 and 2004 approximately, 30.1%, 29.8% and 28.4%, respectively of the plan assets consisted of Rollins, Inc. Common Stock. Total administrative fees for the plan were approximately $159 thousand in 2006, $240 thousand in 2005 and $248 thousand in 2004.

For the year ended December 31, 2006, the Company has issued approximately 0.7 million shares of common stock upon exercise of stock options by employees. For the year ended December 31, 2005, the Company issued approximately 1.2 million shares of common stock upon exercise of stock options by employees.

Stock options and time lapse restricted shares (TLRSs) have been issued to officers and other management employees under the Company's Employee Stock Incentive Plan. The stock options generally vest over a five-year period and expire ten years from the issuance date.

TLRSs provide for the issuance of a share of the Company's Common Stock at no cost to the holder and generally vest after a certain stipulated number of years from the grant date, depending on the terms of the issue. The Company issued TLRSs that vest over ten years prior to 2004. TLRSs issued 2004 and later vest in 20 percent increments starting with the second anniversary of the grant, over six years from the date of grant. During these years, grantees receive all dividends declared and retain voting rights for the granted shares. The agreements under which the restricted stock is issued provide that shares awarded may not be sold or otherwise transferred until restrictions established under the plans have lapsed.

The Company issues new shares from its authorized but unissued share pool. At December 31, 2006, approximately 4.1 million shares of the Company's common stock were reserved for issuance. Effective January 1, 2006, the Company adopted Statement of Financial Accounting Standards No. 123 (revised 2004), Share-Based Payment ("SFAS 123R"), which requires the Company to measure the cost of employee services received in exchange for all equity awards granted including stock options and TLRSs based on the fair market value of the award as of the grant date. SFAS 123R supersedes Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," and Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB 25"). The Company has adopted SFAS 123R using the modified prospective application method of adoption which requires the Company to record compensation cost related to unvested stock awards as of December 31, 2005 by recognizing the unamortized grant date fair value of these awards over the remaining service periods of those awards with no change in historical reported earnings. Awards granted after December 31, 2005 are

valued at fair value in accordance with provisions of SFAS 123R and recognized on a straight line basis over the service periods of each award. The Company estimated forfeiture rates for 2006 based on its historical experience.

Prior to 2006, the Company accounted for stock-based compensation in accordance with APB 25 using the intrinsic value method, which did not require that compensation cost be recognized for the Company's stock options provided the option exercise price was established at 100% of the common stock fair market value on the date of grant. Under APB 25, the Company was required to record expense over the vesting period for the fair value of TLRSs granted. Prior to 2006, the Company provided pro forma disclosure, as if the fair value method defined by SFAS No. 123 had been applied to its stock-based compensation. The Company's net income and net income per share for the year ended December 31, 2005 would have been reduced if compensation cost related to stock options had been recorded in the financial statements based on fair value at the grant dates.

In order to estimate the fair value of stock options, the Company used the Black-Scholes option valuation model, which was developed for use in estimating the fair value of publicly traded options which have no vesting restrictions and are fully transferable. Option valuation models require the input of highly subjective assumptions and these assumptions can vary over time.

The only options outstanding at December 31, 2006 for SFAS 123R purposes are the grants issued during the first quarters of 2002 and 2003. The Company did not grant any stock options in any years following the 2003 grant; therefore no Black-Scholes calculation was necessary.

As a result of adopting SFAS 123R, the impact to the Consolidated Financial Statements for Net Income for the year ended December 31, 2006 was $0.9 million (net of $0.6 million tax benefit) lower, than if the Company had continued to account for stock-based compensation under APB 25. There was no impact to both basic and diluted earnings per share for the year ended December 31, 2006. Pro forma net income as if the fair value based method had been applied to all awards as of December 31, 2005 is as follows:

The following pro forma net income and earnings per share (or "EPS") for 2004 and 2005 were determined as if the Company had accounted for employee stock options and stock issued under its employee stock plans using the fair value method prescribed by SFAS 123. The 2006 actuals are presented for comparative purposes only.

	Twelve months ended December 31,		
(in thousands except per share data)	**2006 as reported**	**2005 pro-forma**	**2004 pro-forma**
Net income as reported	**$ 57,809**	$ 52,773	$ 52,055
Add: Stock-based compensation programs recorded as expense, net of tax		739	260
Deduct: Total stock-based employee compensation expense, net of tax		(1,423)	(1,061)
Pro forma net income		$ 52,089	$ 51,254
Earnings per share:			
Basic income per common share	**$ 0.86**	$ 0.78	$ 0.76
Diluted income per common shares	**0.84**	$ 0.76	$ 0.74
Pro forma basic income per common share		$ 0.77	$ 0.75
Pro forma diluted income per common shares		$ 0.75	$ 0.73

	Twelve months ended December 31,

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The following table summarizes the components of the Company's stock-based compensation programs recorded as expense ($ in thousands):

	Twelve months ended December 31,		
	2006	**2005**	**2004**
Time Lapse Restricted Stock:			
Pre-tax compensation expense	**$ 2,075**	$ 1,244	$ 437
Tax benefit	**(804)**	(505)	(177)
Restricted stock expense, net of tax	**$ 1,271**	$ 739	$ 260
Stock options:			
Pre-tax compensation expense	**$ 912**	$	$
Tax benefit	**(353)**		
Stock option expense, net of tax	**$ 559**	$	$
Total Share-Based Compensation:			
Pre-tax compensation expense	**$ 2,987**	$ 1,244	$ 437
Tax benefit	**(1,157)**	(505)	(177)
Total share-based compensation expense, net of tax	**$ 1,830**	$ 739	$ 260

As of December 31, 2006, $9.9 million and $0.4 million of total unrecognized compensation cost related to time lapse restricted shares and stock options, respectively, is expected to be recognized over a weighted average period of approximately 4.5 years for TLRSs and 1.0 years for stock options.

Option activity under the Company's stock option plan as of December 31, 2006 and changes during the year ended December 31, 2006 were as follows:

	Shares	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Term (in years)**	**Aggregate Intrinsic Value**
Outstanding at December 31, 2003	4,686	$ 8.87	5.79	28,871
Exercised	(721)	8.10		
Forfeited	(208)	10.18		
Outstanding at December 31, 2004	3,757	$ 8.95	4.96	32,262
Exercised	(1,170)	8.23		
Forfeited	(47)	10.69		
Outstanding at December 31, 2005	2,539	$ 9.24	3.98	26,574
Exercised	(688)	8.90		
Forfeited	(67)	9.32		
Outstanding at December 31, 2006	1,784	9.38	4.39	22,715
Exercisable at December 31, 2006	1,406	8.98	4.10	18,470

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of 2006 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders

had all option holders exercised their options on December 31, 2006. The amount of aggregate intrinsic value will change based on the fair market value of the Company's stock.

The aggregate intrinsic value of options exercised during the years ended December 31, 2006 and December 31, 2005 was $8.1 million and $12.5 million, respectively. Exercise of options during the year ended December 31, 2006 and 2005 resulted in cash receipts of $1.1 million and $3.3 million, respectively.

The following table summarizes information on unvested restricted stock units outstanding as of December 31, 2006:

	Number of Shares (in thousands)	Weighted-Average Grant-Date Fair Value
Unvested Restricted Stock Units		
Unvested as of December 31, 2003	70	10.32
Forfeited	(3)	12.43
Vested	(28)	12.50
Granted	228	16.90
Unvested as of December 31, 2004	267	15.99
Forfeited	(11)	15.07
Vested	(4)	10.14
Granted	225	16.44
Unvested as of December 31, 2005	477	16.68
Forfeited	(15)	16.84
Vested	(55)	15.51
Granted	296	21.17
Unvested as of December 31, 2006	703	18.26

9. ACCUMULATED OTHER COMPREHENSIVE INCOME/(LOSS)

Accumulated other comprehensive income/(loss) consist of the following (in thousands):

	Minimum Pension Liability	Foreign Currency Translation	Other Unrealized Gain/(Loss)	Total
Balance at December 31, 2003	$	$ (247)	$ (67)	$ (314)
Change during 2004:				
Before-tax amount	(32,124)	3,967	109	(28,048)
Tax benefit (expense)	13,769	(1,559)	86	12,296
	(18,355)	2,408	195	(15,752)
Balance at December 31, 2004	(18,355)	2,161	128	(16,066)
Change during 2005:				
Before-tax amount	(13,833)	1,114		(12,719)
Tax benefit (expense)	5,652		(131)	5,521
	(8,181)	1,114	(131)	(7,198)

	Minimum Pension Liability	Foreign Currency Translation	Other Unrealized Gain/(Loss)	Total
Balance at December 31, 2005	(26,536)	3,275	(3)	(23,264)
Change during 2006:				
Before-tax amount	9,674	169		9,843
Tax benefit (expense)	(3,957)	(406)		(4,363)
	5,717	(237)		5,480
Balance at December 31, 2006	**$ (20,819)**	**$ 3,038**	**$ (3)**	**$ (17,784)**

10. RELATED PARTY TRANSACTIONS

On April 28, 2004, the Company sold real estate in Okeechobee County, Florida to LOR, Inc., a company controlled by R. Randall Rollins, Chairman of the Board of Rollins, Inc. and Gary W. Rollins, Chief Executive Officer, President and Chief Operating Officer of Rollins, Inc. for $16.6 million in cash. The sale resulted in a net gain after tax of $8.1 million or $0.11 per share since the real estate had appreciated over approximately 30 years it had been owned by the Company. The Company deferred a portion of the gain pending the completion of a survey that may result in the return of a portion of the proceeds. The real estate was under a lease agreement with annual rentals of $131,939 that would have expired June 30, 2007. On May 28, 2004, the Company sold real estate in Sussex County, Delaware to LOR, Inc. for $111,000 in cash. The sale resulted in an immaterial net gain after tax. The Board of Directors, at its quarterly meeting on January 27, 2004, approved the formation of a committee (the "Committee") made up of Messrs. Bill J. Dismuke and James B. Williams, who are independent directors, to evaluate the transactions. In addition, the Company on October 22, 2004 purchased real estate located at 2158 Piedmont Road, N.E., Atlanta, Georgia 30324, adjacent to the Company's headquarters, from LOR, Inc. for $4.6 million. The Committee was furnished with full disclosure of the transactions, including independent appraisals, and determined that the terms of the transactions were reasonable and fair to the Company. The Company sold an additional piece of real estate in Sussex County, Delaware to LOR, Inc. or an entity wholly owned by LOR, Inc. The transaction took place on December 29, 2004 and resulted in a $6.3 million, net of costs, gain after taxes.

The Company provides certain administrative services and rents office space to RPC, Inc. ("RPC") (a company of which Mr. R. Randall Rollins is also Chairman and which is otherwise affiliated with the Company). The service agreements between RPC and the Company provide for the provision of services on a cost reimbursement basis and are terminable on six months notice. The services covered by these agreements include office space, administration of certain employee benefit programs, and other administrative services. Charges to RPC (or to corporations which are subsidiaries of RPC) for such services and rent totaled to $70,000 in 2006, $71,000 in 2005 and $76,000 in 2004.

11. UNAUDITED QUARTERLY DATA

All earnings per share data for the quarters have been restated for the three-for-two stock split effective March 10, 2005.

(in thousands except per share data)	First	Second	Third	Fourth
2006				
Revenues	$ 194,187	$ 232,222	$ 227,816	$ 204,653
Gross Profit (Revenues Cost of Services Provided)	87,173	113,187	108,610	92,039
Net Income	10,903	19,330	17,037	10,539
Income per Share:				
Income per Share Basic	0.16	0.29	0.25	0.16
Income per Share Diluted	0.16	0.28	0.25	0.15
2005				
Revenues	$ 183,915	$ 214,326	$ 209,346	$ 194,830
Gross Profit (Revenues Cost of Services Provided)	85,277	103,732	102,948	88,477
Net Income	11,596	18,725	15,100	7,352
Income per Share:				
Income per Share Basic	0.17	0.28	0.22	0.11
Income per Share Diluted	0.17	0.27	0.22	0.11

12. CASH DIVIDEND

The Board of Directors, at its quarterly meeting on January 23, 2007, authorized a 20% increase in the Company's quarterly dividend. The increased regular quarterly dividend of $0.075 per share will be payable March 12, 2007 to stockholders of record at the close of business February 12, 2007. The Company's new annual dividend rate is $0.30 per share.

13. ACQUISITIONS

On October 1, 2005, the Company acquired substantially all of the assets and assumed certain liabilities of the Industrial Fumigant Company ("IFC") for $23.5 million in cash. The Company's consolidated statements of income include the results of operations of IFC for all periods after October 1, 2005. As a result of the acquisition, the Company recorded $11.5 million in goodwill and $7.8 million in identifiable intangibles, primarily customer contracts.

On April 30, 2004, the Company acquired substantially all of the assets and assumed certain liabilities of Western Pest Services ("Western"). The Company's consolidated financial statements include the operating results of Western from the date of the acquisition. Neither Western nor its principals had any prior relationship with the Company or its affiliates. Western was engaged in the business of providing pest control and termite services and the Company intends to continue this business. The acquisition was made pursuant to an Asset Purchase Agreement (the "Western Agreement") dated March 8, 2004, between Rollins, Inc. and Western Industries, Inc. and affiliates. The consideration for the assets and certain non-competition agreements (the "Purchase Price") was approximately $110.2 million, including approximately $8.4 million of assumed liabilities. The Purchase Price was funded with cash on hand, the sale of property located in Okeechobee County, Florida and a $15.0 million senior unsecured revolving credit facility.

Pursuant to the Western Agreement, the Company acquired substantially all of Western's property and assets, including accounts receivable, real property leases, seller contracts, governmental authorizations, data and records, intangible rights and property and insurance benefits. As described in the Western Agreement, the Company assumed only specified liabilities of Western and obligations under disclosed assigned contracts.

The Company engaged an independent valuation firm to determine the allocation of the Western purchase price. Such valuation resulted in the allocation of $40.8 million to Goodwill and indefinite lived intangible assets and $49.8 million to other intangible assets, principally customer contracts. The finite-lived intangible assets, principally customer contracts, are being amortized over periods principally ranging from 8 to 12.5 years on a straight-lined basis. The total amount of goodwill recorded as a result of the acquisition is expected to be tax deductible over the appropriate periods.

On April 30, 2004, in a transaction ancillary to the Western acquisition, the Company acquired Residex Corporation ("Residex"), a company that distributes chemicals and other products to pest management professionals, pursuant to an Asset Purchase Agreement (the "Residex Agreement") dated March 8, 2004, between Rollins, Inc. and Western Industries, Inc., JBD Incorporated and Residex Corporation. Subsequently on April 30, 2004, the Company sold Residex to an industry distribution group. The amounts involved were not material and no gain or loss was recognized on the transaction.

Significant Acquisition The fair values of Western's assets and liabilities at the date of acquisition are presented below:

Real Estate	$	11,170
Customer Contracts		49,300
Trade Name		5,700
Patents		130
Non Compete Agreement		400
Goodwill		35,106
		101,806
Net Liabilities Assumed		8,357
Net Purchase Price	$	110,163

Pro Forma Results (Unaudited)

The pro forma financial information for 2004 presented below gives effect to the Western acquisition as if it had occurred as of the beginning of fiscal year 2004. The information presented below is for illustrative purposes only and is not necessarily indicative of results that would have been achieved if the acquisition actually had occurred as of the beginning of such year or results, which may be achieved in the future.

	Twelve Months Ended December 31,					
		2006 as reported		**2005 as reported**		**2004 pro-forma**
REVENUES						
Customer Services	**$**	**858,878**	$	802,417	$	776,872
INCOME BEFORE INCOME TAXES AND CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE		**95,159**		87,955		99,453
INCOME BEFORE CUMULATIVE EFFECT OF CHANGE IN ACCOUNTING PRINCIPLE	**$**	**57,809**	$	52,773	$	58,718
INCOME PER SHARE BASIC	**$**	**0.86**	$	0.78	$	0.86
INCOME PER SHARE DILUTED	**$**	**0.84**	$	0.76	$	0.84
Weighted Average Shares Outstanding Basic		**67,165**		67,898		68,321
Weighted Average Shares Outstanding Diluted		**68,876**		69,772		70,167

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosures.

None

Item 9A. Controls and Procedures

Evaluation of Disclosure Controls and Procedures We have established disclosure controls and procedures to ensure, among other things, that material information relating to the Company, including its consolidated subsidiaries, is made known to the officers who certify the Company's financial reports and to other members of senior management and the Board of Directors.

Based on management's evaluation as of December 31, 2006, in which the principal executive officer and principal financial officer of the Company participated, the principal executive officer and principal financial officer have concluded that the Company's disclosure controls and procedures (as defined in

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Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) are effective, at the reasonable assurance level to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms.

Management's Report on Internal Control Over Financial Reporting Management's Report on Internal Control Over Financial Reporting is contained on page 74.

Changes in Internal Controls There were no changes in our internal control over financial reporting during the fourth quarter of 2006 that materially affected or are reasonably likely to materially affect these controls.

Item 9B. Other Information

As previously reported in the Company's Form 8-K filed on October 30, 2006, on October 24, 2006, the Company expanded the Board of Directors to 7 members and appointed Dr. Thomas J. Lawley, M.D., to fill the new seat as a Class III director. Dr. Lawley is the Dean of the Emory University School of Medicine. Various charitable contributions have been made by the O. Wayne Rollins Foundation to Emory University in the past, including charitable contributions made by the Foundation to the Emory University School of Medicine and to the Emory University School of Public Health. Gary W. Rollins, the Chief Executive Officer of the Company, is a director of Emory University.

PART III

Item 10. Directors, Executive Officers and Corporate Governance.

Information concerning directors and executive officers is included in the Company's Proxy Statement for its 2007 Annual Meeting of Stockholders (the "Proxy Statement"), in the section titled "Election of Directors". This information is incorporated herein by reference. Information about executive officers is contained on page 22 of this document.

Audit Committee and Audit Committee Financial Expert

Information concerning the Audit Committee of the Company and the Audit Committee Financial Expert(s) is included in the Company's Proxy Statement, in the section titled "Corporate Governance and Board of Directors Compensation, Committees and Meetings." This information is incorporated herein by reference.

Code of Ethics

The Company has adopted a code of Business Conduct that applies to all employees. In addition, the Company has adopted a Supplemental Code of Business Conduct and Ethics for directors, the Principal Executive Officer and Principal Financial and Accounting Officer. Both of these documents are available on the Company's website at www.rollins.com and a copy is available by writing to Investor Relations at 2170 Piedmont Road, Atlanta Georgia 30324.

Section 16(a) Beneficial Ownership Reporting Compliance

Information regarding compliance with Section 16(a) of the Exchange Act is included under "Compliance with Section 16(a) of the Securities Exchange Act" in the Company's Proxy Statement, which is incorporated herein by reference.

Item 11. Executive Compensation.

The information under the caption "Executive Compensation" included in the Proxy Statement is incorporated herein by reference.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The information under the captions "Capital Stock", "Stock Ownership of Certain Beneficial Owners and Management" and "Election of Directors" and "Equity Compensation Plan Information" included in the Proxy Statement for the Annual Meeting of Stockholders to be held April 24, 2007 is incorporated herein by reference.

EQUITY COMPENSATION PLAN INFORMATION

The following table sets forth certain information regarding equity compensation plans as of December 31, 2006.

Plan Category	Number of Securities To Be Issued Upon Exercise of Outstanding Options, Warrants and Rights (A)	Weighted Average Exercise Price of Outstanding Options, Warrants and Rights (B)	Number of Securities Remaining Available for Future Issuance Under Equity Compensation Plans (Excluding Securities Reflected in Column (A)) (C)
Equity compensation plans approved by security holders	2,262,217	$ 9.50	525,898
Equity compensation plans not approved by security holders	225,000(1)	$ 8.51	
Total	2,487,217	$ 9.38	525,898(2)

(1) These stock options were granted to Mr. Gary W. Rollins, Chief Executive Officer of Rollins, Inc., on January 22, 2002. The total amount of the grant was 450,000, after adjusting for all stock splits to date. However, the Company's 1998 Employee Stock Incentive Plan under which these options were granted stated that no one person may receive in any one year over 225,000 in options. (Mr. Rollins' option grant was for 450,000 shares.) Therefore, the excess is deemed not issued under a security holder approved equity compensation plan. Shares issued upon exercise of these options must be of treasury shares.

(2) Includes 525,898 shares available for grant under the 1998 Employee Stock Incentive Plan. The 1998 Employee Stock Incentive Plan provides for awards of the Company's common stock and awards that are valued in whole or in part by reference to the Company's common stock apart from stock options and SARs including, without limitation, restricted stock, performance-accelerated restricted stock, performance stock, performance units, and stock awards or options valued by reference to book value or subsidiary performance.

Item 13. Certain Relationships and Related Transactions, and Director Independence.

The information under the caption "Certain Relationships and Related Party Transactions" included in the Proxy Statement is incorporated herein by reference. Information concerning director independence is included in the Proxy Statement, in the section titled "Corporate Governance and Board of Directors' Committees and Meetings." This information is incorporated herein by reference.

Item 14. Principal Accounting Fees and Services.

Information regarding principal accounting fees and services is set forth under "Principal Accounting Fees and Services" in the Company's Proxy Statement for its 2007 Annual Meeting of Stockholders, which information is incorporated herein by reference.

PART IV

Item 15. Exhibits and Financial Statement Schedules.

(a) *Consolidated Financial Statements, Financial Statement Schedule and Exhibits.*

1. Consolidated financial statements listed in the accompanying Index to Consolidated Financial Statements and Schedule are filed as part of this report.

2. The financial statement schedule listed in the accompanying Index to Consolidated Financial Statements and Schedule is filed as part of this report.

3. Exhibits listed in the accompanying Index to Exhibits are filed as part of this report. The following such exhibits are management contracts or compensatory plans or arrangements:

(10)(a)	Rollins, Inc. 1994 Employee Stock Incentive Plan incorporated herein by reference to Exhibit (10)(b) as filed with its Form 10-K for the year ended December 31, 1999.
(10)(b)	Rollins, Inc. 1998 Employee Stock Incentive Plan incorporated herein by reference to Exhibit A of the March 24, 1998 Proxy Statement for the Annual Meeting of Stockholders held on April 28, 1998.
(10)(c)	Rollins, Inc. Form of Restricted Stock Agreement incorporated herein by reference to Exhibit (10)(c) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(d)	Rollins, Inc. Form of Option Agreement incorporated herein by reference to Exhibit (10)(d) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(e)	Rollins, Inc. Executive Compensation Summary as of February 28, 2005, incorporated herein by reference to Exhibit (10)(e) as filed with its Form 10-Q for the quarter ended March 31, 2005.
(10)(f)	Written Description of Rollins, Inc. Performance-Based Incentive Cash Compensation Plan incorporated herein by reference to Exhibit (10)(f) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(g)	Form A of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(g) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(h)	Form B of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(h) as filed with its Form 10-Q for the year ended March 31, 2005.
(10)(i)	Summary of Rollins, Inc. Non-Employee Directors Compensation as of February 28, 2005, incorporated herein by reference to Exhibit (10)(i) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(l)	Rollins, Inc. Executive Compensation Summary as of January 24, 2006 incorporated herein by reference to Exhibit (10)(l) as filed with its Form 10-K for the year ended December 31, 2005

(10)(m) Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.1 filed with the registrant's Form S-8 filed November 18, 2005.

(10)(n) Form of Plan Agreement pursuant to the Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.2 filed with the registrant's Form S-8 filed November 18, 2005.

(10)(o) Form A of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(o) as filed with its Form 10-K for the year ended December 31, 2005.

(10)(p) Form B of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(p) as filed with its Form 10-K for the year ended December 31, 2005.

(10)(q) Rollins, Inc. Executive Compensation Summary as of January 23, 2007

(10)(r) Amendment to 1994 and 1998 Stock Incentive Plans

(10)(s) Summary of Rollins, Inc. Non-Employee Directors Compensation as of January 23, 2007

(b)

Exhibits (inclusive of item 3 above):

(2)(a) Asset Purchase Agreement by and among Orkin, Inc. and Western Industries, Inc., Western Exterminating Company, Inc. et al. dated March 8, 2004 incorporated herein by reference to Exhibit (2)(i) as filed with its Form 10-Q for the quarter ended March 31, 2004, as amended.*

(3)(i) (A) Restated Certificate of Incorporation of Rollins, Inc. dated July 28, 1981, incorporated herein by reference to Exhibit (3)(i)(A) as filed with the registrant's Form 10-Q filed August 1, 2005.

(B) Certificate of Amendment of Certificate of Incorporation of Rollins, Inc. dated August 20, 1987, incorporated herein by reference to Exhibit 3(i)(B) filed with the registrant's 10-K filed March 11, 2005.

(C) Certificate of Change of Location of Registered Office and of Registered Agent dated March 22, 1994, incorporated herein by reference to Exhibit (3)(i)(C) filed with the registrant's Form 10-Q filed August 1, 2005.

(D) Certificate of Amendment of Certificate of Incorporation of Rollins, Inc. dated April 25, 2006, incorporated herein by reference to Exhibit 3(i)(D) filed with the registrant's 10-Q filed October 31, 2006

(ii) Revised By-laws of Rollins, Inc. dated March 2, 2004, incorporated herein by reference to Exhibit (3)(ii) as filed with its Form 10-Q for the quarterly period ended March 31, 2004.

(4) Form of Common Stock Certificate of Rollins, Inc. incorporated herein by reference to Exhibit (4) as filed with its Form 10-K for the year ended December 31, 1998.

(10)(a) Rollins, Inc. 1994 Employee Stock Incentive Plan incorporated herein by reference to Exhibit (10)(b) as filed with its Form 10-K for the year ended December 31, 1999.

(10)(b) Rollins, Inc. 1998 Employee Stock Incentive Plan incorporated herein by reference to Exhibit A of the March 24, 1998 Proxy Statement for the Annual Meeting of Stockholders held on April 28, 1998.

(10)(c) Rollins, Inc. Form of Restricted Stock Agreement incorporated herein by reference to Exhibit (10)(c) as filed with its Form 10-K for the year ended December 31, 2004.

(10)(d)	Rollins, Inc. Form of Option Agreement incorporated herein by reference to Exhibit (10)(d) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(e)	Rollins, Inc. Executive Compensation Summary as of February 28, 2005, incorporated herein by reference to Exhibit (10)(e) as filed with its Form 10-Q for the quarter ended March 31, 2005.
(10)(f)	Written Description of Rollins, Inc. Performance-Based Incentive Cash Compensation Plan incorporated herein by reference to Exhibit (10)(f) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(g)	Form A of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(g) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(h)	Form B of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(h) as filed with its Form 10-Q for the year ended March 31, 2005.
(10)(i)	Summary of Rollins, Inc. Non-Employee Directors Compensation as of February 28, 2005, incorporated herein by reference to Exhibit (10)(i) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(j)	Purchase and Sale Agreement by and among Rollins Continental, Inc. et al. dated April 28, 2004 incorporated herein by reference to Exhibit (2)(ii) as filed with its Form 10-Q for the quarter ended June 30, 2004.
(10)(k)	Purchase and Sale Agreement by and among Rollins Continental, Inc. et al. dated December 20, 2004 incorporated herein by reference to Exhibit (10)(k) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(l)	Rollins, Inc. Executive Compensation Summary as of January 24, 2006 incorporated herein by reference to Exhibit (10)(l) as filed with its Form 10-K for the year ended December 31, 2005
(10)(m)	Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.1 filed with the registrant's Form S-8 filed November 18, 2005.
(10)(n)	Form of Plan Agreement pursuant to the Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.2 filed with the registrant's Form S-8 filed November 18, 2005.
(10)(o)	Form A of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(o) as filed with its Form 10-K for the year ended December 31, 2005.
(10)(p)	Form B of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(p) as filed with its Form 10-K for the year ended December 31, 2005.
(10)(q)	Rollins, Inc. Executive Compensation Summary as of January 23, 2007
(10)(r)	Amendment to 1994 and 1998 Stock Incentive Plans
(10)(s)	Summary of Rollins, Inc. Non-Employee Directors Compensation as of January 23, 2007
(21)	Subsidiaries of Registrant.

(23.1)	Consent of Grant Thornton LLP, Independent Registered Public Accounting Firm.
(24)	Powers of Attorney for Directors.
(31.1)	Certification of Chief Executive Officer Pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(31.2)	Certification of Chief Financial Officer Pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(32.1)	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*

Confidential treatment, pursuant to 17 C.F.R. Sections 200.80 and 230.406, has been granted regarding certain portions of the indicated Exhibit, which portions have been filed separately with the Commission.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

ROLLINS, INC.

By: /s/ GARY W. ROLLINS

Gary W. Rollins
Chief Executive Officer, President and Chief Operating Officer
(Principal Executive Officer)

Date: February 27, 2007

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the Registrant and in the capacities and on the dates indicated.

/s/ GARY W. ROLLINS

Gary W. Rollins
Chief Executive Officer, President and Chief Operating Officer
(Principal Executive Officer)

Date: February 27, 2007

By: /s/ HARRY J. CYNKUS

Harry J. Cynkus
Chief Financial Officer and Treasurer
(Principal Financial and Accounting Officer)

Date: February 27, 2007

The Directors of Rollins, Inc. (listed below) executed a power of attorney appointing Gary W. Rollins their attorney-in-fact, empowering him to sign this report on their behalf.

R. Randall Rollins, Director
Wilton Looney, Director
Henry B. Tippie, Director
James B. Williams, Director
Bill J. Dismuke, Director
Thomas J. Lawley, Director

/s/ GARY W. ROLLINS

Gary W. Rollins
As Attorney-in-Fact & Director
February 27, 2007

ROLLINS, INC. AND SUBSIDIARIES
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND SCHEDULE
(Item 15)

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(2) *Financial Statement Schedules*	
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Schedules not listed above have been omitted as not applicable, immaterial or disclosed in the Consolidated Financial Statements or notes thereto.

SCHEDULE II VALUATION AND QUALIFYING ACCOUNTS

ROLLINS, INC. AND SUBSIDIARIES

(in thousands)	**Balance at Beginning of Period**	**Charged to Costs and Expenses**	**Net (Deductions) Recoveries**	**Balance at End of Period**
Year ended December 31, 2006				
Allowance for doubtful accounts	$ 5,615	$ 7,195	$ (5,582)(1)	$ 7,228
Year ended December 31, 2005				
Allowance for doubtful accounts	$ 5,108	$ 5,796	$ (5,289)(1)	$ 5,615
Year ended December 31, 2004				
Allowance for doubtful accounts	$ 4,616	$ 5,552	$ (5,060)(1)	$ 5,108

(1) Net deductions represent the write-off of uncollectible receivables, net of recoveries and transfer in of reserves from Superior, Western and IFC acquisitions.

ROLLINS, INC. AND SUBSIDIARIES INDEX TO EXHIBITS

Exhibit Number	Exhibit Description
(2)(a)	Asset Purchase Agreement by and among Orkin, Inc. and Western Industries, Inc., Western Exterminating Company, Inc. et al. dated March 8, 2004 incorporated herein by reference to Exhibit (2)(i) as filed with its Form 10-Q for the quarter ended March 31, 2004, as amended. *
(3)(i)	(A) Restated Certificate of Incorporation of Rollins, Inc. dated July 28, 1981, incorporated herein by reference to Exhibit (3)(i)(A) as filed with the registrant's Form 10-Q filed August 1, 2005.
	(B) Certificate of Amendment of Certificate of Incorporation of Rollins, Inc. dated August 20, 1987, incorporated herein by reference to Exhibit 3(i)(B) filed with the registrant's 10-K filed March 11, 2005.
	(C) Certificate of Change of Location of Registered Office and of Registered Agent dated March 22, 1994, incorporated herein by reference to Exhibit (3)(i)(C) filed with the registrant's Form 10-Q filed August 1, 2005.
	(D) Certificate of Amendment of Certificate of Incorporation of Rollins, Inc. dated April 25, 2006, incorporated herein by reference to Exhibit 3(i)(D) filed with the registrant's 10-Q filed October 31, 2006
(ii)	Revised By-laws of Rollins, Inc. dated March 2, 2004, incorporated herein by reference to Exhibit (3)(ii) as filed with its Form 10-Q for the quarterly period ended March 31, 2004.
(4)	Form of Common Stock Certificate of Rollins, Inc. incorporated herein by reference to Exhibit (4) as filed with its Form 10-K for the year ended December 31, 1998.
(10)(a)	Rollins, Inc. 1994 Employee Stock Incentive Plan incorporated herein by reference to Exhibit (10)(b) as filed with its Form 10-K for the year ended December 31, 1999.
(10)(b)	Rollins, Inc. 1998 Employee Stock Incentive Plan incorporated herein by reference to Exhibit A of the March 24, 1998 Proxy Statement for the Annual Meeting of Stockholders held on April 28, 1998.
(10)(c)	Rollins, Inc. Form of Restricted Stock Agreement incorporated herein by reference to Exhibit (10)(c) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(d)	Rollins, Inc. Form of Option Agreement incorporated herein by reference to Exhibit (10)(d) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(e)	Rollins, Inc. Executive Compensation Summary as of February 28, 2005, incorporated herein by reference to Exhibit (10)(e) as filed with its Form 10-Q for the quarter ended March 31, 2005.
(10)(f)	Written Description of Rollins, Inc. Performance-Based Incentive Cash Compensation Plan incorporated herein by reference to Exhibit (10)(f) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(g)	Form A of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(g) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(h)	Form B of Executive Bonus Plan for Fiscal Year 2005 incorporated herein by reference to Exhibit (10)(h) as filed with its Form 10-Q for the year ended March 31, 2005.

(10)(i)	Summary of Rollins, Inc. Non-Employee Directors Compensation as of February 28, 2005, incorporated herein by reference to Exhibit (10)(i) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(j)	Purchase and Sale Agreement by and among Rollins Continental, Inc. et al. dated April 28, 2004 incorporated herein by reference to Exhibit (2)(ii) as filed with its Form 10-Q for the quarter ended June 30, 2004.
(10)(k)	Purchase and Sale Agreement by and among Rollins Continental, Inc. et al. dated December 20, 2004 incorporated herein by reference to Exhibit (10)(k) as filed with its Form 10-K for the year ended December 31, 2004.
(10)(l)	Rollins, Inc. Executive Compensation Summary as of January 24, 2006 incorporated herein by reference to Exhibit (10)(l) as filed with its Form 10-K for the year ended December 31, 2005
(10)(m)	Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.1 filed with the registrant's Form S-8 filed November 18, 2005.
(10)(n)	Form of Plan Agreement pursuant to the Rollins, Inc. Amended and Restated Deferred Compensation Plan, incorporated herein by reference to Exhibit 4.2 filed with the registrant's Form S-8 filed November 18, 2005.
(10)(o)	Form A of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(o) as filed with its Form 10-K for the year ended December 31, 2005.
(10)(p)	Form B of Executive Bonus Plan incorporated herein by reference to Exhibit (10)(p) as filed with its Form 10-K for the year ended December 31, 2005.
(10)(q)	Rollins, Inc. Executive Compensation Summary as of January 23, 2007
(10)(r)	Amendment to 1994 and 1998 Stock Incentive Plans
(10)(s)	Summary of Rollins, Inc. Non-Employee Directors Compensation as of January 23, 2007
(21)	Subsidiaries of Registrant.
(23.1)	Consent of Grant Thornton LLP, Independent Registered Public Accounting Firm.
(24)	Powers of Attorney for Directors.
(31.1)	Certification of Chief Executive Officer Pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(31.2)	Certification of Chief Financial Officer Pursuant to Item 601(b)(31) of Regulation S-K, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
(32.1)	Certification of Chief Executive Officer and Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

*

Confidential treatment, pursuant to 17 C.F.R. Sections 200.80 and 230.406, has been granted regarding certain portions of the indicated Exhibit, which portions have been filed separately with the Commission.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON CONSOLIDATED FINANCIAL STATEMENTS

Board of Directors and Stockholders
of Rollins, Inc.

We have audited the accompanying consolidated balance sheets of Rollins, Inc. (a Delaware corporation) and subsidiaries (the "Company") as of December 31, 2006 and 2005, and the related consolidated statements of income, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Rollins, Inc. and subsidiaries as of December 31, 2006 and 2005, and the consolidated results of its operations and its consolidated cash flows for each of the three years in the period ended December 31, 2006 in conformity with accounting principles generally accepted in the United States of America.

Our audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. Schedule II, as listed in the Index on page 69, is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. This schedule has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

As described in Note 1 to the consolidated financial statements, the Company adopted the recognition provisions of Statement of Financial Accounting Standards No. 158, "Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans, an amendment of FASB Statements No. 87, 88, 106, and 132(R)" and also the provisions of Statement of Financial Accounting Standards No. 123 (revised 2004), "Share-Based Payment" during 2006 and changed its method of accounting for the revenues and costs associated with conventional termite renewal contracts in 2004.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Rollins, Inc. and subsidiaries' internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) and our report dated February 26, 2007 expressed an unqualified opinion.

/s/ GRANT THORNTON LLP

Atlanta, Georgia
February 26, 2007

MANAGEMENT'S REPORT ON INTERNAL CONTROLS OVER FINANCIAL REPORTING

To the Stockholders of Rollins, Inc.:

The management of Rollins, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting for the Company. Rollins maintains a system of internal accounting controls designed to provide reasonable assurance, at a reasonable cost, that assets are safeguarded against loss or unauthorized use and that the financial records are adequate and can be relied upon to produce financial statements in accordance with accounting principles generally accepted in the United States of America. The internal control system is augmented by written policies and procedures, an internal audit program and the selection and training of qualified personnel. This system includes policies that require adherence to ethical business standards and compliance with all applicable laws and regulations.

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of the effectiveness of the design and operations of internal controls over financial reporting, as of December 31, 2006 based on criteria established in Internal Control Integrated framework issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management's assessment is that Rollins, Inc. maintained effective internal control over financial reporting as of December 31, 2006.

The independent registered public accounting firm, Grant Thornton LLP, who has audited the consolidated financial statements for the year ended December 31, 2006, included in the 2005 annual report, have also issued their report on management's assessment of the Company's internal control over financial reporting.

/s/ GARY W. ROLLINS

Gary W. Rollins
Chief Executive Officer, President and Chief Operating Officer
Atlanta, Georgia
February 27, 2007

/s/ HARRY J. CYNKUS

Harry J. Cynkus
Chief Financial Officer and Treasurer

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Board of Directors and Stockholders of Rollins, Inc.

We have audited management's assessment included in Management's Report on Internal Controls Over Financial Reporting included in Rollins, Inc's. (a Delaware Corporation) and subsidiaries (the "Company") Form 10-K for 2006, that the Company maintained effective internal control over financial reporting as of December 31, 2006 based on criteria established in Internal Control Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The Company's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting. Our responsibility is to express an opinion on management's assessment and an opinion on the effectiveness of the company's internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, evaluating management's assessment, testing and evaluating the design and operating effectiveness of internal control, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, management's assessment that the Company maintained effective internal control over financial reporting as of December 31, 2006, is fairly stated, in all material respects, based on criteria established in Internal Control Integrated Framework issued by the COSO. Also in our opinion, the Company maintained, in all material respects, effective internal control over financial reporting as of December 31, 2006, based on criteria established in Internal Control Integrated Framework issued by the COSO.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of the Company as of December 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2006 and our report dated February 26, 2007 expressed an unqualified opinion on those financial statements.

/s/ GRANT THORNTON LLP

Atlanta, Georgia
February 26, 2007

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