

Special Opportunities Fund, Inc.  
Annual Report  
For the year ended  
December 31, 2011



# Special Opportunities Fund, Inc.

February 11, 2012

Dear Fellow Shareholders:

In 2011 the stock market was about as volatile as in any year we can recall. Big daily moves, both up and down, were frequent. The Fund's net asset value was off 4.99% in the second half of the year vs. -3.69% for the S&P 500 Index. In the end, the market was little changed in 2011. For the year, the Fund posted a modest NAV gain of 0.85% (assuming reinvested dividends), slightly less than the S&P 500 Index which rose 2.11%.

Although Special Opportunities Fund is not intended to be market neutral, we are risk averse. Consequently, in the third quarter when the market hit its lows, the Fund was well ahead of the S&P 500 Index. Given its heavy weighting in special purpose acquisition companies (SPACs), auction rate preferred stock (ARPs) issued by closed-end funds, bankruptcy claims, and other investments that are not highly correlated with the stock market, we think our performance in 2011 was pretty good.

We believe that preserving capital in down markets is more important to generating superior long term results than beating the market when the wind is at our back. Until we find a reliable crystal ball, we will continue to treat the market as an unpredictable beast. As always, our focus is on investing where we think we have an edge and using activism when necessary to try to unlock the value of our investments. The following discussion of a few of our investments should give you some insight into how we try to meet the Fund's objective of generating solid total returns over time without incurring inordinate risk.

## **Gyrodyne Corporation of America (GYRO)**

In June 2010, a trial court awarded GYRO about \$70 per share (based upon the current share count) plus 9% statutory interest for property that New York State appropriated in 2005. After the decision was issued, GYRO's stock price quickly moved from the upper \$30's to more than \$70 per share. Even though most savvy investors fully expected the state to appeal, the euphoria faded after the appeal was actually filed. Despite no change in the status of the case, by mid-summer last year GYRO's stock price had drifted down to the \$60's. It then fell into the \$50's when a rights offering at \$53 per share was announced. The rights offering was designed to raise cash to maintain GYRO's remaining rental properties. We added to our position via the rights offering which concluded on September 22, 2011.

The state's case for overturning the award appeared weak. In the trial, the state argued that GYRO's property could never be used for residential use and that it should be given a much lower valuation based upon light industrial zoning. The trial court disagreed. It ruled that residential use was feasible and yielded the highest valuation. Having failed to present any evidence relating to the property's

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value for residential use, the state asked the appellate court to order a second trial to allow it to present such evidence.

Oral argument in the appellate court took place on October 24th. The following week the stock price moved from \$61 to \$79 on heavy volume, indicating optimism that the appeal would fail. That optimism proved to be correct. On November 23rd, the appellate court unanimously upheld the lower court's ruling. Since then, the stock price has been hovering around \$100 per share. In late December the state filed a petition for a further appeal to the Court of Appeals, the state's highest court. Nevertheless, we think the risk-reward ratio is attractive at current levels because the appellate court's decision was unanimous although there is a slim possibility that the judges of the Court of Appeals could be influenced by New York's dire fiscal condition.

With most of the uncertainty removed, this investment has little downside risk in our opinion. If, as we expect, the Court of Appeals declines to review the case, we would expect the state to make payment of about \$106 per share (including interest) shortly thereafter. Until it does, interest accrues at about 70 cents per share per month. As a REIT, Gyrodyne will have to distribute the accrued interest of about \$40 per share to avoid double taxation. Management has also publicly committed to pursue a liquidity event. Therefore, we would expect a merger or sale of the company to yield another \$75 to \$85 per share in 2012 or 2013.

## **TS&W/Claymore Tax-Advantage Balanced Fund (TYW)**

This hybrid fund's objective was total return and current income through investment in municipal and equity securities. We accumulated a sizeable position at a discount to NAV after another activist investor conducted an aggressive proxy contest in 2010. A majority of the shares were voted for the activist's slate of directors but a quorum was not achieved so the incumbent directors retained control. Nevertheless, the writing was on the wall. On April 15, 2011, TYW announced that it would open-end, which we felt was inevitable. We continued to opportunistically accumulate shares of this low beta fund right up until it ceased trading on December 30, 2011. TYW open-ended on January 17, 2012 and we redeemed all of our shares at NAV. This was a very successful relatively low risk investment.

## **SunAmerica Asset Management Funds (FGF and FGI)**

In 2009 these sister funds traded at discounts in excess of 15%. In order to forestall a proxy contest, management agreed to conduct an in-kind tender offer for 30% and 25% respectively of the outstanding shares at 98.5% of NAV. The tender offers were completed in November 2010. Faced with continuing shareholder unrest over their persistent discounts, the board of each fund announced that it intended to convert it to an open-end fund redeemable at NAV less a 1% charge in late January 2012. We continued to opportunistically add to our positions at discounts slightly wider than 1%. Both funds became eligible for

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redemption on January 24th and we are now completely out of them. All in all, these were two very successful investments.

## **Liberty All-Star Growth Fund (ASG) and Liberty All-Star Equity Fund (USA)**

These are well diversified multi-manager equity funds. ASG currently trades at about a 10% discount and USA at about a 13% discount. In late July 2011, the funds announced that shareholders would vote on September 30, 2011 to approve a new management agreement due to a change of control of the funds' manager. That vote passed but only because the new manager paid a premium to buy a significant number of shares from a large shareholder. To mollify shareholders that were miffed about what they perceived to be "greenmail," we think there is a good chance that management will initiate a value enhancing liquidity event in 2012. If that does not happen, the Fund may participate in a proxy fight. In any event, these two funds allow us to get broad market exposure at a discount to NAV while we wait.

## **The New Ireland Fund (IRL)**

IRL is a relatively small (\$53 million in NAV) closed-end fund whose shares usually trade within a discount range of 9% to 14%. Special Opportunities Fund is part of a group that currently owns almost 13% of IRL's outstanding shares. Last year, we met with IRL's management to discuss measures to enhance shareholder value. Since then, the board hired a consultant "to prepare an analysis of discount-narrowing measures, which may be appropriate for the Fund." We are hopeful for an outcome beneficial to the Fund and all IRL shareholders sometime in 2012.

## **Auction Rate Preferred Shares**

Over the last two years, we purchased a significant amount of ARPs issued by closed-end funds at 80 to 85% of face value. These securities are extremely safe but have become very hard to sell since the auction market collapsed in early 2008. However, because the Investment Company Act of 1940 requires that two directors be elected by the preferred shareholders as a class, we perceived a chance to use our activist approach to investing to unlock their intrinsic value. Due largely to our proactive approach, we have had favorable developments recently with respect to our three largest ARPs positions.

- **Blackrock New York Municipal Bond Trust (BQH)** – Special Opportunities Fund was a member of a group that purchased 22% of the ARPs at about 85% of face value. Blackrock had previously made some efforts to redeem the ARPs issued by many of its closed-end funds. Progress then slowed. When Blackrock refused to allow us to nominate a director to represent the preferred shareholders, we sued the BQH board in Delaware Chancery Court. Two months later, we reached a settlement in which Blackrock committed to nominate a candidate of our choice to the board in 2012 if the ARPs have not been redeemed. In October 2011, all of our ARPs were redeemed.

# Special Opportunities Fund, Inc.

- Federated Premier Intermediate Municipal Income Fund (FPT) – We nominated a director who would commit to explore measures to provide liquidity for the holders of ARPs. In December 2011, FPT conducted a self-tender offer for up to 100% of its ARPs at 96% of their liquidation value. We tendered our shares and booked a nice profit.
- Invesco Quality Municipal Investment Trust (IQT) – As with FPT, we nominated a director and entered into discussions with management about providing liquidity for holders of the ARPs. We then agreed to withdraw our nomination because we felt management was acting in good faith to address the problem. On December 7, 2011, IQT announced that it would redeem a portion of its outstanding ARPs in the first quarter of 2012 at their liquidation value. That redemption recently took place. We are optimistic that all of our ARPs will ultimately be redeemed.

## **Diamond Hill Financial Trends Fund (DHFT)**

This is a good illustration of how we seek to execute our opportunistic activist investment philosophy. DHFT is a small \$40 million closed-end fund that invests in the securities of financial services companies. Its top five holdings, Wells Fargo, JP Morgan, Assured Guarantee, U.S. Bancorp and PNC — represent almost 30% of its net asset value.

DHFT began its existence in 1989 as the Southeastern Thrift and Bank Fund. Its name was later changed to John Hancock Financial Trends Fund. In September 2007, Diamond Hill replaced John Hancock as the manager and the name changed again. While the discount for DHFT has often been wide, we avoided making an investment because of a quirk in its corporate governance. Unlike most closed-end funds, DHFT's shares were listed on NASDAQ which did not require closed-end funds to hold an annual meeting. And, to the best of our knowledge, DHFT never held one. Therefore, it would have been very difficult to bring sufficient pressure to bear on management and the board to take measures to address the discount.

Finally, in 2011, NASDAQ changed its rules and now requires all listed companies to hold an annual shareholder meeting. With that impediment removed, we began to rapidly accumulate shares at about a 15% discount late in the third quarter. We became even more aggressive just before we had to make a public filing with the result that our filing group now owns almost 15% of DHFT's shares. The current discount is about 10%. We have contacted management and the board to discuss the discount and we are optimistic that they will be responsive. If that does not happen, we have several options to press our case, given the fund's small size.

## **SPACs**

SPACs or blank check companies make up a large portion of our portfolio. These misunderstood investments are probably the safest equity investments around

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because the money raised in the IPO is held in a trust account. In addition, there is upside potential via the “free” warrants we receive in the IPO. We think we can earn an average of between 5% and 15% per annum on our entire portfolio of SPACs with virtually no risk to our principal. Thus far, there has been little news from the latest batch of SPACs. However, a number of them are slated to terminate in 2012 unless they consummate a transaction so we expect to see some announcements of proposed transactions in the first half of this year.

## **New Opportunities**

The pipeline for future alpha generating investments is robust. The Fund has been accumulating stock in several closed-end funds that are trading at double-digit discounts and are good targets for activism because their performance has been very poor. It takes time to accumulate a large enough position to begin a campaign to unlock value but we hope to pick up the pace after completion of the planned rights offering. As yet, we have not publicly disclosed any of these potential targets but we are confident that some or all of them will ultimately provide the Fund with true alpha, i.e., unleveraged risk-adjusted outperformance.

In addition, we have been building a position in one operating company that is trading at a significant discount to cash and has recently taken steps to maximize shareholder value. Finally, we, along with our affiliates, have accumulated a meaningful stake in a financial company that is trading for less than half of its intrinsic value due to potential legal problems. We have met with management and feel that the problems can be resolved over time and that the depressed stock price more than compensates for them. We expect to “go public” on both of these investments eventually and will likely have more to say about them in future letters.

In conclusion, we do not believe there is a holy grail of investment success. Nothing works all the time. To us, investing is like running a marathon. In both cases, it is important to have a long term plan that is unlikely to lead to catastrophic losses when things go wrong from time to time, as inevitably happens. Our long term strategy is to stay within striking distance of the market when it moves up and to pass it when it falters. By avoiding market calls and investment fads, and by executing our value activist strategy in a disciplined fashion, we will try hard to provide shareholders of Special Opportunities Fund with superior long term risk-adjusted performance.

Sincerely yours,



Phillip Goldstein  
Chairman

# Special Opportunities Fund, Inc.

## Performance at a glance (unaudited)

### Average annual total returns for common stock for the periods ended 12/31/11

Net asset value returns	1 year	Since 1/25/10	5 years*	10 years*
Special Opportunities Fund, Inc.	0.85%	8.19%	4.80%	5.12%

### Market price returns

Special Opportunities Fund, Inc.	1.89%	7.02%	5.60%	5.96%
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### Index returns

S&P 500 Index	2.11%	9.59%	-0.25%	2.92%
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### Share price as of 12/31/11

Net asset value	\$16.01
Market price	\$14.50

**Past performance does not predict future performance. The return and value of an investment will fluctuate so that an investor's share, when sold, may be worth more or less than their original cost. The Fund's common stock net asset value ("NAV") return assumes, for illustration only, that dividends and other distributions, if any, were reinvested at the NAV on payable dates for dividends and other distributions payable through December 31, 2009 and reinvested at the NAV on the ex-dividend date for dividends and other distributions payable after December 31, 2009. The Fund's common stock market price returns assume that all dividends and other distributions, if any, were reinvested at prices obtained under the Fund's Dividend Reinvestment Plan (which was terminated on January 1, 2010) for dividends and other distributions payable through December 31, 2009 and reinvested at the lower of the NAV or the closing market price on the ex-dividend date for dividends and other distributions payable after December 31, 2009. NAV and market price returns for the period of less than one year have not been annualized. Returns do not reflect the deduction of taxes that a shareholder could pay on Fund dividends and other distributions, if any, or the sale of Fund shares.**

\* The Fund's investment objective and investment adviser have changed. See Note 1 of the Notes to financial statements for more information about the change in investment objective and see Note 2 of the Notes to financial statements for more information about the change in investment adviser. On January 25, 2010, the Fund began investing using its new investment objective, therefore, performance prior to that date is not relevant.

The S&P 500 Index is a capital weighted, unmanaged index that represents the aggregate market value of the common equity of 500 stocks primarily traded on the New York Stock Exchange.

# Special Opportunities Fund, Inc.

## Portfolio composition as of 12/31/11<sup>(1)</sup>

	Value	Percent
Investment Companies	\$ 71,617,683	67.02%
Common Stocks	29,751,370	27.84
Corporate Bonds	4,507,750	4.22
Money Market Funds	3,852,469	3.60
Structured Life Settlement Notes	876,583	0.82
Warrants	766,409	0.72
<b>Total Investments</b>	<b>\$111,372,264</b>	<b>104.22%</b>
Liabilities in Excess of Other Assets	(4,508,672)	(4.22)
<b>Total Net Assets</b>	<b>\$106,863,592</b>	<b>100.00%</b>

<sup>(1)</sup> As a percentage of net assets.

# Special Opportunities Fund, Inc.

## Portfolio of investments—December 31, 2011

	Shares	Value
<b>INVESTMENT COMPANIES—67.02%</b>		
<b>Closed-End Funds—51.66%</b>		
Adams Express Company	276,839	\$ 2,668,728
Alpine Global Premier Properties Fund	785,585	4,163,601
American Strategic Income Portfolio III	159,466	1,039,718
Bancroft Fund, Ltd.	41,401	625,983
BlackRock Credit Allocation Income Trust IV	55,854	678,626
Boulder Growth & Income Fund, Inc.	316,668	1,817,674
Boulder Total Return Fund, Inc.	184,149	2,780,650
Diamond Hill Financial Trends Fund, Inc.	39,736	328,617
Dividend & Income Fund, Inc.	11,112	38,114
DWS RREEF Real Estate Fund, Inc. (a)(c)(f)(g)	126,913	11,803
DWS RREEF Real Estate Fund II, Inc. (a)(c)(f)(g)	201,612	28,830
Eaton Vance Risk Managed Diversified Equity Income Fund	244,645	2,556,540
Federated Enhanced Treasury Income Fund	4,532	65,034
First Opportunity Fund, Inc. (a)	279,106	1,736,039
Firsthand Technology Value Fund, Inc. (a)	2,373	34,527
The GDL Fund	33,327	393,259
The Greater China Fund, Inc.	55,714	561,040
JF China Region Fund, Inc.	1,885	20,754
Liberty All-Star Equity Fund, Inc.	1,437,759	6,067,342
Liberty All-Star Growth Fund, Inc.	349,392	1,331,184
Macquarie Global Infrastructure Total Return Fund, Inc.	80,776	1,372,384
Morgan Stanley Asia Pacific Fund, Inc.	30,101	394,323
Neuberger Berman Real Estate Securities Income Fund, Inc.	5,257	19,714
The New Ireland Fund, Inc.	188,171	1,298,380
Royce Focus Trust, Inc.	17,500	110,250
Royce Micro-Cap Trust, Inc.	440,426	3,862,536
Royce Value Trust, Inc.	348,093	4,271,101
Shelton Greater China Fund (a)	82,342	489,935
SunAmerica Focused Alpha Growth Fund, Inc.	244,426	4,468,107
SunAmerica Focused Alpha Large-Cap Fund, Inc.	41,507	673,659
Tri-Continental Corporation	387,319	5,511,549
TS&W/Claymore Tax-Advantaged Balanced Fund	321,385	3,756,991
The Zweig Total Return Fund, Inc.	670,639	2,032,036
		55,209,028
<b>Auction Rate Preferred Securities—13.24% (b)(c)</b>		
BlackRock California Municipal 2018 Term Trust - Series M7, 0.152%	100	2,250,000
BlackRock Municipal 2018 Term Trust - Series W7, 0.168%	100	2,250,000

# Special Opportunities Fund, Inc.

## Portfolio of investments—December 31, 2011

	Shares	Value
<b>INVESTMENT COMPANIES—(continued)</b>		
<b>Auction Rate Preferred Securities—(continued)</b>		
BlackRock Municipal Bond Trust - Series R7, 0.152%	75	\$ 1,875,000
BlackRock Municipal Bond Trust - Series T7, 0.183%	75	1,875,000
BlackRock Municipal Income Quality Trust - Series F7, 0.220%	60	1,500,000
BlackRock MuniHoldings Fund, Inc. - Series C, 1.316%	25	625,000
BlackRock MuniHoldings Fund II, Inc. - Series A, 0.183%	50	1,250,000
Invesco Quality Municipal Investment Trust - Series A, 0.033%	53	2,385,000
MFS High Yield Municipal Trust - Series F, 0.152%	1	18,750
Western Asset Premier Bond Fund - Series M, 0.060%	6	120,000
		14,148,750
<b>Business Development Company—2.12%</b>		
Capital Southwest Corporation	1,468	119,715
Equus Total Return, Inc. (a)	106,919	239,499
MVC Capital, Inc.	163,994	1,900,691
		2,259,905
<b>Total Investment Companies (Cost \$69,413,003)</b>		<b>71,617,683</b>
<b>COMMON STOCKS—27.84%</b>		
<b>Life Insurance—0.23%</b>		
Imperial Holdings, Inc. (a)	129,047	242,608
<b>Oil and Gas Field Exploration Services—0.03%</b>		
Zion Oil & Gas, Inc. (a)	14,090	31,139
<b>Pharmaceuticals Preparations—0.60%</b>		
Myrexis, Inc. (a)	240,861	645,507
<b>Real Estate Investment Trusts—1.53%</b>		
American Realty Capital Properties, Inc.	60,000	624,000
Gyrodyne Company of America, Inc. (a)	9,942	1,014,084
		1,638,084
<b>Special Purpose Acquisition Vehicle—25.45%</b>		
Australia Acquisition Corporation (a)	250,000	2,450,000
Azteca Acquisition Corporation (a)	189,924	1,813,774
Blue Wolf Mongolia Holdings Corporation (a)	50,273	483,626
Cazador Acquisition Corporation, Ltd. (a)	200,000	1,956,000
China Growth Equity Investment, Ltd. (a)	52,798	502,109
China VantagePoint Acquisition Company (a)(i)	27,130	160,610
Empeiria Acquisition Corp. (a)	182,343	1,779,668

# Special Opportunities Fund, Inc.

## Portfolio of investments—December 31, 2011

	Shares	Value
<b>COMMON STOCKS—(continued)</b>		
<b>Special Purpose Acquisition Vehicle—(continued)</b>		
FlatWorld Acquisition Corporation (a)(h)	105,702	\$ 1,059,134
Global Cornerstone Holdings, Ltd. (a)(h)	115,935	1,159,350
Global Eagle Acquisition Corporation (a)	54,028	517,048
Hicks Acquisition Company II, Inc. (a)	248,537	2,403,353
JWC Acquisition Corporation (a)	377,578	3,681,386
L&L Acquisition Corporation (a)	100,000	991,000
Lone Oak Acquisition Corporation (a)	81,430	631,083
Nautilus Marine Acquisition Corporation (a)	127,846	1,224,764
Prime Acquisition Corporation (a)	65,008	619,526
RLJ Acquisition, Inc. (a)	312,788	2,980,870
SCG Financial Acquisition Corporation (a)	154,865	1,455,731
Selway Capital Acquisition Corp. (a)	80,000	744,000
Universal Business Payment Solutions Acquisition Corporation (a)	100,000	581,000
		27,194,032
<b>Total Common Stocks (Cost \$29,288,892)</b>		<b>29,751,370</b>

	Principal Amount	
<b>CORPORATE BONDS—4.22%</b>		
Washington Mutual, Inc.		
0.000%, 09/17/2012 (d)	\$3,000,000	3,022,500
5.250%, 09/15/2017 (d)	1,300,000	1,485,250
<b>Total Corporate Bonds (Cost \$4,458,185)</b>		<b>4,507,750</b>

<b>STRUCTURED LIFE SETTLEMENT NOTES—0.82%</b>		
Cedar Lane Series A-2 Notes (c)(f)	876,583	876,583
<b>Total Structured Life Settlement Notes (Cost \$876,583)</b>		<b>876,583</b>

	Shares	
<b>WARRANTS—0.72%</b>		
Australia Acquisition Corporation		
Expiration: October 2015		
Exercise Price: \$11.50 (a)	250,000	92,500
Azteca Acquisition Corporation		
Expiration: April 2018		
Exercise Price: \$12.50 (a)	189,924	75,970

# Special Opportunities Fund, Inc.

## Portfolio of investments—December 31, 2011

	Shares	Value
<b>WARRANTS—(continued)</b>		
Blue Wolf Mongolia Holdings Corporation Expiration: July 2016 Exercise Price: \$12.00 (a)	50,273	\$ 30,164
Cazador Acquisition Corporation, Ltd. Expiration: October 2015 Exercise Price: \$7.50 (a)	228,491	45,697
China Growth Equity Investment, Ltd. Expiration: February 2013 Exercise Price: \$12.00 (a)	52,798	22,175
Empeiria Acquisition Corporation Expiration: December 2017 Exercise Price: \$11.50 (a)	182,343	38,292
FlatWorld Acquisition Corporation Expiration: September 2012 Exercise Price: \$11.00 (a)	30,248	7,562
Hicks Acquisition Company II, Inc. Expiration: July 2017 Exercise Price: \$12.00 (a)	200,000	62,000
JWC Acquisition Corporation Expiration: November 2015 Exercise Price: \$11.50 (a)	150,000	75,000
L&L Acquisition Corporation Expiration: November 2015 Exercise Price: \$11.50 (a)	100,000	55,000
Lone Oak Acquisition Corporation Expiration: March 2016 Exercise Price: \$5.00 (a)	81,430	20,358
Nautilus Marine Acquisition Corporation Expiration: July 2016 Exercise Price: \$11.50 (a)	127,846	31,962
Prime Acquisition Corporation Expiration: March 2016 Exercise Price: \$7.50 (a)	51,442	12,861
RLJ Acquisition, Inc. Expiration: February 2016 Exercise Price: \$12.00 (a)	353,462	123,711
SCG Financial Acquisition Corporation Expiration: May 2016 Exercise Price: \$11.50 (a)	154,865	38,716
Selway Cap Acquisition Corporation Expiration: November 2016 Exercise Price: \$0.75 (a)	80,000	9,600

# Special Opportunities Fund, Inc.

## Portfolio of investments—December 31, 2011

	Shares	Value
<b>WARRANTS—(continued)</b>		
Universal Business Payment Solutions Acquisition Corporation		
Expiration: May 2017		
Exercise Price: \$6.90 (a)	100,000	\$ 20,000
Zion Oil & Gas, Inc.		
Expiration: August 2012		
Exercise Price: \$3.50 (a)	20,170	4,841
<b>Total Warrants (Cost \$933,314)</b>		<b>766,409</b>
<b>MONEY MARKET FUNDS—3.60%</b>		
Fidelity Institutional Government Portfolio - Class I, 0.01% (e)	1,766,313	1,766,313
Fidelity Institutional Tax-Exempt Portfolio - Class I, 0.01% (e)	2,086,155	2,086,156
Total Money Market Funds (Cost \$3,852,469)		<b>3,852,469</b>
Total Investments (Cost \$108,822,446)—104.22%		111,372,264
Liabilities in Excess of Other Assets—(4.22)%		(4,508,672)
<b>TOTAL NET ASSETS—100.00%</b>		<b>\$ 106,863,592</b>

Percentages are stated as a percent of net assets.

- (a) Non-income producing security.
- (b) The coupon rates shown represent the rates at December 31, 2011.
- (c) Fair valued securities. The total market value of these securities was \$15,065,966, representing 14.10% of net assets.
- (d) Default or other conditions exist and security is not presently accruing income.
- (e) The rate shown represents the 7-day yield at December 31, 2011.
- (f) Illiquid security. The total market value of these securities was \$917,216 representing 0.86% of net assets.
- (g) Security currently undergoing a full liquidation with all proceeds paid out to shareholders.
- (h) Each unit consists of one share of common stock and one warrant.
- (i) Each unit consists of one share of common stock, one half of a non-transferrable warrant and one half of a transferrable warrant.

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# Special Opportunities Fund, Inc.

## Statement of assets and liabilities—December 31, 2011

### Assets:

Investments, at value (cost—\$108,822,446)	\$ 111,372,264
Cash	622,573
Dividends and interest receivable	234,767
Receivable for investments sold	36,138
Other assets	18,939
Total assets	112,284,681

### Liabilities:

Payable for investments purchased	1,646,024
Distributions payable	3,574,905
Payable to Adviser	91,644
Accrued expenses and other liabilities	108,516
Total liabilities	5,421,089
Net assets applicable to common shareholders	\$ 106,863,592

### Net assets applicable to common shareholders:

Common stock—\$0.001 par value per common share; 199,995,800 shares authorized; 6,676,450 shares issued and outstanding, 13,951,913 shares held in treasury	\$ 301,974,125
Cost of shares held in treasury	(197,838,117)
Accumulated undistributed net investment income	—
Accumulated net realized gain from investment activities	177,766
Net unrealized appreciation of investments	2,549,818
Net assets applicable to common shareholders	\$ 106,863,592
Net asset value per common share (\$106,863,592 applicable to 6,676,450 common shares outstanding)	\$16.01

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

# Special Opportunities Fund, Inc.

## Statement of operations

	For the year ended December 31, 2011
<b>Investment income:</b>	
Dividends	\$3,008,431
Interest	133,666
Total investment income	3,142,097
<b>Expenses:</b>	
Investment advisory fees	1,113,338
Professional fees and expenses	183,467
Directors' fees and expenses	114,040
Administration fees and expenses	90,850
Compliance fees and expenses	37,602
Accounting fees and expenses	36,675
Insurance fees	25,773
Stock exchange listing fees	25,318
Reports and notices to shareholders	25,189
Custody fees and expenses	14,011
Transfer agency fees and expenses	12,888
Other expenses	3,388
Total expenses	1,682,539
Net investment income	1,459,558
<b>Net realized and unrealized gains (losses) from investment activities:</b>	
Net realized gains from:	
Investments	5,411,750
Distributions received from investment companies	252,696
Net change in unrealized depreciation of investments	(6,316,741)
Net realized and unrealized losses from investment activities	(652,295)
Net increase in net assets applicable to common shareholders resulting from operations	\$ 807,263

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

# Special Opportunities Fund, Inc.

## Statement of cash flows

For the  
year ended  
December 31, 2011

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**Cash flows from operating activities:**

Net increase in net assets applicable to common shareholders \$ 807,263

Adjustments to reconcile net increase in net assets applicable to common shareholders  
resulting from operations to net cash provided by operating activities:

Purchases of investments (64,691,465)

Proceeds from sales of investments 60,141,047

Net purchases and sales of short-term investments 1,543,652

Amortization and accretion of premium and discount (9,874)

Return of capital dividends 23,211

Decrease in dividends and interest receivable 180,624

Decrease in receivable for investments sold 312,142

Increase in other assets (1,176)

Increase in payable for investments purchased 1,452,616

Increase in payable to Adviser 19

Decrease in payable to directors (671)

Decrease in accrued expenses and other liabilities (39,900)

Net realized gains from investments (5,411,750)

Net change in unrealized depreciation of investments 6,316,741

Net cash provided by operating activities 622,479

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**Cash flows from financing activities:**

Cash dividends paid to common shareholders —

Net cash used in financing activities —

Net change in cash \$622,479

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**Cash:**

Beginning of year 94

End of year \$ 622,573

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

# Special Opportunities Fund, Inc.

## Statements of changes in net assets applicable to common shareholders

	For the year ended December 31, 2011	For the year ended December 31, 2010
<b>From operations:</b>		
Net investment income	\$ 1,459,558	\$ 288,602
Net realized gains from investments and distributions received from investment companies	5,664,446	4,381,868
Net change in unrealized appreciation (depreciation) of investments	(6,316,741)	8,866,559
Net increase in net assets resulting from operations	807,263	13,537,029
<b>Dividends paid to common shareholders from:</b>		
Net investment income	(1,760,646)	(200,293)
Net realized gains from investment activities	(1,814,259)	—
Total dividends and distributions paid to common shareholders	(3,574,905)	(200,293)
<b>Capital Share Transactions (Note 5):</b>		
Repurchase of common stock through tender offer	—	(197,838,117)
Net decrease in net assets from capital share transactions	—	(197,838,117)
Net decrease in net assets applicable to common shareholders	(2,767,642)	(184,501,381)
<b>Net assets applicable to common shareholders:</b>		
Beginning of year	109,631,234	294,132,615
End of year	\$106,863,592	\$109,631,234
Accumulated undistributed net investment income	\$ —	\$ 273,788

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

# Special Opportunities Fund, Inc.

## Financial highlights

Selected data for a share of common stock outstanding throughout each period is presented below:

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**Net asset value, beginning of period**

Net investment income

Net realized and unrealized gains (losses) from investment activities

Common share equivalent of dividends and distributions paid to auction preferred shareholders from:  
Net investment income

Net realized gains from investment activities

Total dividends and distributions paid to auction preferred shareholders

Net increase (decrease) from operations

Dividends and distributions paid to common shareholders from:

Net investment income

Net realized gains from investment activities

Total dividends and distributions paid to common shareholders

**Net asset value, end of period****Market value, end of period**

**Total net asset value return<sup>(3)</sup>**

**Total market price return<sup>(4)</sup>**

**Ratio to average net assets attributable to common shares:**

Total expenses, net of fee waivers by investment advisor and administrator including interest expense and fees on floating rate notes

Total expenses, before fee waivers by investment advisor and administrator including interest expense and fees on floating rate notes

Total expenses, net of fee waivers by investment advisor and administrator excluding interest expense and fees on floating rate notes

Net investment income before dividends paid to auction preferred shareholders

Dividends paid to auction preferred shareholders from net investment income

Net investment income available to common shareholders

**Supplemental data:**

Net assets applicable to common shareholders, end of period (000's)

Portfolio turnover

Asset coverage per share of auction preferred shares, end of period

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For the years ended December 31,		For the nine months ended December 31, 2009	For the years ended March 31,		
2011	2010		2009	2008	2007
\$16.42	\$14.26	\$13.05	\$13.71	\$14.96	\$14.70
0.22 <sup>(1)(2)</sup>	0.04 <sup>(1)(2)</sup>	0.52 <sup>(1)</sup>	0.88 <sup>(1)</sup>	0.97 <sup>(1)</sup>	0.94 <sup>(1)</sup>
(0.10)	2.15	1.24	(0.70)	(1.22)	0.33
—	—	(0.02)	(0.25)	(0.39)	(0.34)
—	—	—	—	(0.01)	(0.02)
—	—	(0.02)	(0.25)	(0.40)	(0.36)
0.12	2.19	1.74	(0.07)	(0.65)	0.91
(0.26)	(0.03)	(0.53)	(0.59)	(0.58)	(0.62)
(0.27)	—	—	—	(0.02)	(0.03)
(0.53)	(0.03)	(0.53)	(0.59)	(0.60)	(0.65)
\$16.01	\$16.42	\$14.26	\$13.05	\$13.71	\$14.96
\$14.50	\$14.75	\$14.09	\$11.37	\$12.38	\$13.48
0.85%	15.36%	13.51%	(0.39)%	(4.52)%	6.31%
1.89%	4.90%	29.00%	(3.32)%	(3.86)%	8.83%
1.51% <sup>(7)</sup>	1.50% <sup>(7)</sup>	1.03% <sup>(5)(6)</sup>	1.73% <sup>(6)</sup>	1.18%	1.25%
1.51% <sup>(7)</sup>	1.67% <sup>(7)</sup>	1.92% <sup>(5)(6)</sup>	2.62% <sup>(6)</sup>	1.88%	1.88%
1.51% <sup>(7)</sup>	1.50% <sup>(7)</sup>	0.99% <sup>(5)</sup>	1.59%	1.18%	1.25%
1.32% <sup>(2)</sup>	0.26% <sup>(2)</sup>	5.00% <sup>(5)</sup>	6.71%	6.66%	6.32%
—	—	0.20% <sup>(5)</sup>	1.87%	2.68%	2.31%
1.32% <sup>(2)</sup>	0.26% <sup>(2)</sup>	4.80% <sup>(5)</sup>	4.84%	3.98%	4.01%
\$106,864	\$109,631	\$294,133	\$269,266	\$282,886	\$308,552
55%	73%	7%	27%	30%	39%
\$ —	\$ —	\$ —	\$136,860	\$117,354	\$123,465

# Special Opportunities Fund, Inc.

## Financial highlights

- <sup>(1)</sup> Calculated using the average shares method.
- <sup>(2)</sup> Recognition of net investment income by the Fund is affected by the timing and declaration of dividends by the underlying investment companies in which the Fund invests.
- <sup>(3)</sup> Total net asset value return is calculated assuming a \$10,000 purchase of common stock at the current net asset value on the first day of each period reported and a sale at the current net asset value on the last day of each period reported, and assuming reinvestment of dividends and other distributions at the net asset value on the payable date for dividends and other distributions payable through December 31, 2009 and reinvested at the NAV on the ex-dividend date for dividends and other distributions payable after December 31, 2009. Total investment return based on net asset value is hypothetical as investors can not purchase or sell Fund shares at net asset value but only at market prices. Returns do not reflect the deduction of taxes that a shareholder could pay on Fund dividends and other distributions, if any, or the sale of Fund shares.
- <sup>(4)</sup> Total market price return is calculated assuming a \$10,000 purchase of common stock at the current market price on the first day of each period reported and a sale at the current market price on the last day of each period reported, and assuming reinvestment of dividends and other distributions to common shareholders at prices obtained under the Fund's Dividend Reinvestment Plan (which was terminated on January 1, 2010) for dividends and other distributions payable through December 31, 2009 and reinvested at the lower of the NAV or the closing market price on the ex-dividend date for dividends and other distributions payable after December 31, 2009. Total investment return does not reflect brokerage commissions and has not been annualized for the period of less than one year. Returns do not reflect the deduction of taxes that a shareholder could pay on Fund dividends and other distributions, if any, or the sale of Fund shares.
- <sup>(5)</sup> Annualized.
- <sup>(6)</sup> Interest expense represents interest and fees on short term floating rate notes issued in conjunction with inverse floating rate securities. Interest income from such transactions was included in income from investment operations.
- <sup>(7)</sup> Does not include expenses of the investment companies in which the Fund invests.

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

# Special Opportunities Fund, Inc.

## Notes to financial statements

### Note 1

#### **Organization and significant accounting policies**

Special Opportunities Fund, Inc. (formerly, Insured Municipal Income Fund Inc.) (the "Fund") was incorporated in Maryland on February 18, 1993, and is registered with the Securities and Exchange Commission under the Investment Company Act of 1940, as amended, as a closed-end diversified management investment company. Effective December 21, 2009, the Fund changed its name to the Special Opportunities Fund, Inc. and changed its investment objective to total return. There can be no assurance that the Fund's investment objective will be achieved. The Fund's previous investment objective was to achieve a high level of current income that was exempt from federal income tax, consistent with the preservation of capital.

In the normal course of business, the Fund may enter into contracts that contain a variety of representations or that provide indemnification for certain liabilities. The Fund's maximum exposure under these arrangements is unknown, as this would involve future claims that may be made against the Fund that have not yet occurred. However, the Fund has not had prior claims or losses pursuant to these contracts and expects the risk of loss to be remote.

The preparation of financial statements in accordance with Accounting Standards Codification Topic 105 Generally Accepted Accounting Principles requires the Fund's management to make estimates and assumptions that affect the reported amounts and disclosures in the financial statements. Actual results could differ from those estimates. In preparing these financial statements, the Fund has evaluated events and transactions for potential recognition or disclosure and has determined that there were no subsequent events requiring recognition or disclosure in the financial statements. The following is a summary of significant accounting policies:

**Valuation of investments**—The Fund calculates its net asset value based on the current market value for its portfolio securities. The Fund normally obtains market values for its securities from independent pricing sources and broker-dealers. Independent pricing sources may use last reported sale prices or if not available the most recent bid price, current market quotations or valuations from computerized "matrix" systems that derive values based on comparable securities. A matrix system incorporates parameters such as security quality, maturity and coupon, and/or research and evaluations by its staff, including review of broker-dealer market price quotations, if available, in determining the valuation of the portfolio securities. If a market value is not available from an independent pricing source or a broker-dealer for a particular security, that security is valued at fair value as determined in good faith by or under the direction of the Fund's Board of Directors (the "Board"). Various factors may be reviewed in order to make a good faith determination of a security's fair value.

# Special Opportunities Fund, Inc.

## Notes to financial statements

The auction rate preferred securities and the structured life settlement notes are valued at cost, unless other observable market events occur. The purchase price, or cost, of these securities is arrived at through an arms length transaction between a willing buyer and seller in the secondary market and is indicative of the value on the secondary market. Current transactions in similar securities in the marketplace are evaluated. Factors for other securities may include, but are not limited to, the type and cost of the security; contractual or legal restrictions on resale of the security; relevant financial or business developments of the issuer; actively traded similar or related securities; conversion or exchange rights on the security; related corporate actions; and changes in overall market conditions. If events occur that materially affect the value of securities between the close of trading in those securities and the close of regular trading on the New York Stock Exchange, the securities may be fair valued. The amortized cost method of valuation, which approximates market value, generally is used to value short-term debt instruments with sixty days or less remaining to maturity, unless the Board or its delegate determines that this does not represent fair value.

The Fund has adopted fair valuation accounting standards that establish an authoritative definition of fair value and set out a hierarchy for measuring fair value. These standards require additional disclosures about the various input and valuation techniques used in measuring fair value. Fair value inputs are summarized in the three broad levels listed below:

- Level 1—Unadjusted quoted prices in active markets for identical assets or liabilities that the Fund has the ability to access.
- Level 2—Observable inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly. These inputs may include quoted prices for the identical instrument on an inactive market, prices for similar instruments, interest rates, prepayment speeds, credit risk, yield curves, default rates and similar data.
- Level 3—Unobservable inputs for the asset or liability, to the extent relevant observable inputs are not available, representing the Fund's own assumptions about the assumptions a market participant would use in valuing the asset or liability, and would be based on the best information available.

The availability of observable inputs can vary from security to security and is affected by a wide variety of factors, including, for example, the type of security, whether the security is new and not yet established in the marketplace, the liquidity of markets, and other characteristics particular to the security. To the extent that valuation is based on models or inputs that are less observable or unobservable in the market, the determination of fair value requires more judgment. Accordingly, the degree of judgment exercised in determining fair value is greatest for instruments categorized in Level 3.

# Special Opportunities Fund, Inc.

## Notes to financial statements

The inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such cases, for disclosure purposes, the level in the fair value hierarchy within which the fair value measurement falls in its entirety, is determined based on the lowest level input that is significant to the fair value measurement in its entirety.

The following is a summary of the fair valuations according to the inputs used as of December 31, 2011 in valuing the Fund's investments:

	<b>Quoted Prices in Active Markets for Identical Investments (Level 1)</b>	<b>Significant Other Observable Inputs (Level 2)</b>	<b>Unobservable Inputs (Level 3)</b>	<b>Total</b>
Investment Companies	\$57,428,300	\$ 40,633	\$14,148,750	\$ 71,617,683
Common Stocks	11,953,248	17,798,122	—	29,751,370
Corporate Bonds	—	4,507,750	—	4,507,750
Structured Life Settlement Notes	—	—	876,583	876,583
Warrants	184,303	582,106	—	766,409
Money Market Funds	3,852,469	—	—	3,852,469
Total	\$73,418,320	\$22,928,611	\$15,025,333	\$111,372,264

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

Balance as of December 31, 2010	\$19,966,625
Accrued discounts / premiums	—
Realized gain (loss)	1,014,812
Change in unrealized appreciation (depreciation)	1,518,063
Purchases	138,750
Sales	(7,612,917)
Transfers in and / or out of Level 3	—
Balance as of December 31, 2011	\$15,025,333

During the year ended December 31, 2011, there were no transfers into and out of Levels 1 and 2. Transfers between levels are recognized at the end of the reporting period.

In May 2011, the FASB issued ASU No. 2011-04 "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements" in GAAP and the International Financial Reporting Standards ("IFRSs"). ASU No. 2011-04 amends FASB ASC Topic 820, Fair Value Measurements and Disclosures, to establish common requirements for measuring fair value and for disclosing information about fair value measurements in accordance with GAAP and IFRSs.

# Special Opportunities Fund, Inc.

## Notes to financial statements

ASU No. 2011-04 is effective for fiscal years beginning after December 15, 2011 and for interim periods within those fiscal years. Management is currently evaluating the impact of these amendments and does not believe they will have a material impact on the Company's financial statements.

In December 2011, FASB issued ASU 2011-11 related to disclosures about offsetting assets and liabilities. The amendments in this ASU require an entity to disclose information about offsetting and related arrangements to enable users of its financial statements to understand the effect of those arrangements on its financial position. The ASU is effective for annual reporting periods beginning on or after January 1, 2013, and interim periods within those annual periods. The guidance requires retrospective application for all comparative periods presented. The Adviser is currently evaluating the impact ASU 2011-11 will have on the financial statement disclosures.

**Concentration risk**—The Fund invested 13.24% of its net assets in auction rate preferred securities as of December 31, 2011. An active market for auction rate preferred securities does not exist. There is no guarantee that the Fund could receive the fair value price for these securities if it tried to sell them in the secondary market.

**Investment transactions and investment income**—Investment transactions are recorded on the trade date. Realized gains and losses from investment transactions are calculated using the identified cost method. Interest income is recorded on an accrual basis. Discounts are accreted and premiums are amortized as adjustments to interest income and the identified cost of investments.

**Dividends and distributions**—Dividends from net investment income and distributions of net realized capital gains, if any, will be declared and paid at least annually. Dividends and distributions to common shareholders are recorded on the ex-dividend date. The amount of dividends from net investment income and distributions from net realized capital gains was determined in accordance with federal income tax regulations, which may differ from U.S. generally accepted accounting principles. These "book/tax" differences are either considered temporary or permanent in nature. To the extent these differences are permanent in nature, such amounts are reclassified within the capital accounts based on their federal tax-basis treatment; temporary differences do not require reclassification.

### Note 2

#### Investment adviser and administrator

Effective October 19, 2009, the Board appointed Brooklyn Capital Management, LLC ("Brooklyn") as the interim investment adviser to the Fund. At a Special Meeting of Shareholders held on December 10, 2009, shareholders approved an

# Special Opportunities Fund, Inc.

## Notes to financial statements

investment advisory agreement between the Fund and Brooklyn. In accordance with the investment advisory agreement, the Fund is obligated to pay Brooklyn a monthly investment advisory fee at an annual rate of 1.00% of the Fund's average weekly net assets. The Fund entered into an administrative services agreement (the "Administration Agreement") with U.S. Bancorp Fund Services, LLC (the "Administrator"), which was effective on October 19, 2009.

### **Note 3**

#### **Auction preferred shares**

The Fund was subject to certain restrictions relating to the APS. Failure to comply with these restrictions could have precluded the Fund from declaring any distributions to common shareholders or repurchasing common shares and/or could have triggered the mandatory redemption of APS at liquidation value.

All APS were redeemed in October 2009.

### **Note 4**

#### **Purchases and sales of securities**

For the year ended December 31, 2011, aggregate purchases and sales of portfolio securities, excluding short-term securities, were \$64,691,465 and \$60,141,047, respectively. The Fund did not have any purchases or sales of U.S. government securities during the year ended December 31, 2011.

### **Note 5**

#### **Capital share transactions**

The Fund did not have any capital share transactions during the year ended December 31, 2011. During the year ended December 31, 2010, a total of 13,951,912 shares or approximately 67.63% of the Fund's outstanding common shares were validly tendered pursuant to a tender offer approved by the Board. All such shares were accepted for payment at a price of \$14.18 per share (99.5% of the NAV per common share of \$14.25).

### **Note 6**

#### **Federal tax status**

The Fund intends to distribute its income and to comply with the other requirements of the Internal Revenue Code applicable to regulated investment companies. Accordingly, no provision for federal income taxes is required. In addition, by distributing during each calendar year substantially all of its net investment income, net realized capital gains and certain other amounts, if any, the Fund would not be subject to a federal excise tax.

# Special Opportunities Fund, Inc.

## Notes to financial statements

The tax character of distributions paid during the fiscal year ended December 31, 2011 and the year ended December 31, 2010 were as follows:

<b>Distributions paid from:</b>	<b>For the year ended December 31, 2011</b>	<b>For the year ended December 31, 2010</b>
Tax-exempt income	\$ —	\$184,078
Ordinary income	1,939,242	16,215
Long-term capital gains	1,635,663	—
Total distributions paid	\$3,574,905	\$200,293

The Fund designated as long-term capital gain dividends, pursuant to Internal Revenue Code Section 852(b)(3), the amount necessary to reduce the earnings and profits for the Fund related to net capital gains to zero for the year ended December 31, 2011.

The following information is presented on an income tax basis as of December 31, 2011:

Tax cost of investments	\$108,864,729
Unrealized appreciation	5,712,186
Unrealized depreciation	(3,204,651)
Net unrealized appreciation	2,507,535
Undistributed ordinary income	40,663
Undistributed long-term gains	179,386
Total distributable earnings	220,049
Other accumulated losses and other temporary differences	—
Total accumulated losses	2,727,584

To reflect reclassifications arising from permanent “book/tax” differences for the year ended December 31, 2011, the Fund’s accumulated undistributed net investment income (loss) was decreased by \$27,300 and accumulated net realized gain from investment activities was decreased by \$27,300.

For the year ended December 31, 2011, the Fund did not have any liabilities for any unrecognized tax positions. The Fund recognizes interest and penalties, if any, related to unrecognized tax positions as income tax expense in the Statement of operations. During the year ended December 31, 2011, the Fund did not incur any interest or penalties.

Each of the tax years in the two year period ended December 31, 2010 and the year ended December 31, 2011 remains subject to examination by the Internal Revenue Service and state taxing authorities.

# Special Opportunities Fund, Inc.

## Notes to financial statements

On December 22, 2010, The Regulated Investment Company Modernization Act of 2010 (the "Modernization Act") was signed by The President. The Modernization Act is the first major piece of legislation affecting Regulated Investment Companies ("RICs") since 1986 and it modernizes several of the federal income and excise tax provisions related to RICs. Some highlights of the enacted provisions are as follows:

New capital losses may now be carried forward indefinitely, and retain the character of the original loss. Under pre-enactment law, capital losses could be carried forward for eight years, and carried forward as short-term capital, irrespective of the character of the original loss.

The Modernization Act contains simplification provisions, which are aimed at preventing disqualification of a RIC for "inadvertent" failures of the asset diversification and/or qualifying income tests. Additionally, the Modernization Act exempts RICs from the preferential dividend rule, and repealed the 60-day designation requirement for certain types of pay-through income and gains.

Finally, the Modernization Act contains several provisions aimed at preserving the character of distributions made by a fiscal year RIC during the portion of its taxable year ending after October 31 or December 31, reducing the circumstances under which a RIC might be required to file amended Forms 1099 to restate previously reported distributions.

Except for the simplification provisions related to RIC qualification, the Modernization Act is effective for taxable years beginning after December 22, 2010. The provisions related to RIC qualification are effective for taxable years for which the extended due date of the tax return is after December 22, 2010.

# Special Opportunities Fund, Inc.

## Report of independent registered public accounting firm

### To the Board of Directors and Shareholders of Special Opportunities Fund, Inc.

We have audited the accompanying statement of assets and liabilities of Special Opportunities Fund, Inc. including the portfolio of investments, as of December 31, 2011, and the related statement of operations and cash flows for the year then ended, the statement of changes in net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended and the nine month period ended December 31, 2009. These financial statements and financial highlights are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements and financial highlights based on our audits. The financial highlights for each of the three years in the period ended March 31, 2009, have been audited by other auditors, whose report dated May 19, 2009 expressed an unqualified opinion on such financial statements and financial highlights.

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 audit to obtain reasonable assurance about whether the financial statements and financial highlights are free of material misstatement. The Fund is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. Our procedures included confirmation of securities owned as of December 31, 2011, by correspondence with the custodian and brokers or by other appropriate auditing procedures where replies from brokers were not received. 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 financial statements and financial highlights referred to above present fairly, in all material respects, the financial position of Special Opportunities Fund, Inc. as of December 31, 2011, the results of its operations and cash flows for the year then ended, the changes in its net assets for each of the two years in the period then ended, and the financial highlights for each of the two years in the period then ended and the nine month period ended December 31, 2009, in conformity with accounting principles generally accepted in the United States of America.

*Tait, Weller & Baker LLP*  
**TAIT, WELLER & BAKER LLP**

**Philadelphia, Pennsylvania**  
**February 16, 2012**

# Special Opportunities Fund, Inc.

## General information (unaudited)

### The Fund

Special Opportunities Fund, Inc. (the "Fund") is a diversified, closed-end management investment company whose common shares trade on the New York Stock Exchange ("NYSE"). The Fund's NYSE trading symbol is "SPE." On April 21, 2010 the Fund's symbol changed from "PIF" to "SPE." Comparative net asset value and market price information about the Fund is available weekly in various publications.

### Annual meeting of shareholders held on December 7, 2011

The Fund held an annual meeting of shareholders on December 7, 2011 to vote on the following matters:

- (1) To elect six directors to serve until the annual meeting of stockholders in 2012 and until their successors are elected and qualify or until they resign or are otherwise removed;
- (2) To instruct the Adviser to vote proxies received by the Fund from any closed-end investment company in the Fund's portfolio on any proposal (including the election of directors) in a manner which the Adviser reasonably determines is likely to favorably impact the discount of such investment company's market price as compared to its net asset value.

### Proxy results

The presence, in person or by proxy, of shareholders entitled to cast a majority of the votes entitled to be cast at the Meeting (i.e., the presence of a majority of the shares outstanding on the record date of October 21, 2011) was necessary to constitute a quorum for the transaction of business. At the Meeting, the holders of approximately 93.16% of the common stock outstanding as of the record date were represented in person or by proxy (6,219,885 votes), thus constituting a quorum for the matters to be voted upon by all shareholders at the Meeting.

The actual voting results for the agenda items were as follows:

#### Proposal to elect James Chadwick as a director:

FOR	% of Quorum	% of O/S	WITHHELD
5,139,593	82.63%	76.98%	1,080,293

#### Proposal to elect Andrew Dakos as a director:

FOR	% of Quorum	% of O/S	WITHHELD
4,940,400	79.43%	74.00%	1,279,486

# Special Opportunities Fund, Inc.

## General information (unaudited)

### Proposal to elect Phillip Goldstein as a director:

FOR	% of Quorum	% of O/S	WITHHELD
5,826,128	93.67%	87.26%	393,758

### Proposal to elect Ben Harris as a director:

FOR	% of Quorum	% of O/S	WITHHELD
6,033,016	97.00%	90.36%	186,870

### Proposal to elect Gerald Hellerman as a director:

FOR	% of Quorum	% of O/S	WITHHELD
5,893,769	94.76%	88.28%	326,117

### Proposal to elect Charles C. Walden as a director:

FOR	% of Quorum	% of O/S	WITHHELD
6,068,608	97.57%	90.90%	151,278

**Proposal to instruct the Adviser to vote proxies received by the Fund from any closed-end investment company in the Fund's portfolio on any proposal (including the election of directors) in a manner which the Adviser reasonably determines is likely to favorably impact the discount of such investment company's market price as compared to its net asset value.**

FOR	% of Quorum	% of O/S	WITHHELD
3,116,846	97.44%	46.68%	37,028

O/S = outstanding shares

### Additional tax information

For the fiscal year ended December 31, 2011, certain dividends paid by the Fund may be subject to a maximum tax rate of 15%, as provided for by the Jobs and Growth Tax Relief Reconciliation Act of 2003. The percentage of dividends declared from ordinary income designated as qualified dividend income was 67%. For corporate shareholders, the percent of ordinary income distributions qualifying for the corporate dividends received deduction for the fiscal year ended December 31, 2011 was 66%. The percentage of taxable ordinary income distributions that are designated as short-term capital gain distributions under Internal Revenue Section 871 (k)(2)(C) for the Fund was 10%.

# Special Opportunities Fund, Inc.

## General information (unaudited)

### **Quarterly Form N-Q portfolio schedule**

The Fund files its complete schedule of portfolio holdings with the Securities and Exchange Commission ("SEC") for the first and third quarters of each fiscal year on Form N-Q. The Fund's Forms N-Q are available on the SEC's Web site at <http://www.sec.gov>. The Fund's Forms N-Q may be reviewed and copied at the SEC's Public Reference Room in Washington, D.C. Information on the operation of the SEC's Public Reference Room may be obtained by calling 1-800-SEC-0330. Additionally, you may obtain copies of Forms N-Q from the Fund upon request by calling 1-877-607-0414.

### **Proxy voting policies, procedures and record**

You may obtain a description of the Fund's (1) proxy voting policies, (2) proxy voting procedures and (3) information regarding how the Fund voted any proxies related to portfolio securities during the most recent 12-month period ended June 30 for which an SEC filing has been made, without charge, upon request by contacting the Fund directly at 1-877-607-0414, or on the EDGAR Database on the SEC's Web site (<http://www.sec.gov>).

# Special Opportunities Fund, Inc.

## Supplemental information (unaudited)

The following table sets forth the directors and officers of the Fund, his name, address, age, position with the Fund, term of office and length of service with the Fund, principal occupation or employment during the past five years and other directorships held at December 31, 2011.

Name, Address and Age*	Position(s) Held with the Fund	Term of Office and Length of Time Served	Principal Occupation During the Past Five Years	Number of Portfolios in Fund Complex Overseen by Director**	Other Directorships held by Director
<b>INTERESTED DIRECTOR</b>					
Andrew Dakos*** (45)	President as of October 2009.	1 year; Since 2009	Principal and Chief Compliance Officer of the Adviser; Principal of the general partner of several private investment partnerships in the Bulldog Investors group of funds.	1	Director, Mexico Equity and Income Fund, Inc.; Director, Brantley Capital Corporation.
Phillip Goldstein*** (66)	Chairman and Secretary as of October 2009.	1 year; Since 2009	Principal of the Adviser; Principal of the general partner of several private investment partnerships in the Bulldog Investors group of funds.	1	Chairman, Mexico Equity and Income Fund, Inc.; Chairman, Brantley Capital Corporation; Director, ASA Ltd; Director, Korea Equity and Income Fund, Inc.
Gerald Hellerman**** (74)	Chief Compliance Officer and Chief Financial Officer as of January 2010.	1 year; Since 2009	Managing Director of Hellerman Associates (a financial and corporate consulting firm).	1	Director, Mexico Equity and Income Fund, Inc.; Director, Brantley Capital Corporation; Director, MVC Capital, Inc.; Director, Old Mutual Absolute Return and Emerging Managers Fund Complex.

# Special Opportunities Fund, Inc.

## Supplemental information (unaudited)

Name, Address and Age*	Position(s) Held with the Fund	Term of Office and Length of Time Served	Principal Occupation During the Past Five Years	Number of Portfolios in Fund Complex Overseen by Director**	Other Directorships held by Director
<b>INDEPENDENT DIRECTORS</b>					
James Chadwick (38)	—	1 year; Since 2009	Managing Director of Main Street Investment Partners, LLC (private equity firm); Managing Director of Opus Partners, LLC (private equity firm); Managing Director of Harlingwood Equity Partners LP; Managing Partner of Chadwick Capital Management.	1	None
Ben Harris (43)	—	1 year; Since 2009	Chief Financial Officer and General Counsel of NHI II, LLC and NBC Bancshares, LLC; Investment Professional of MVC Capital, Inc. and The Tokarz Group Advisers, LLC.	1	None
Charles C. Walden (67)	—	1 year; Since 2009	President and Owner of Sound Capital Associates, LLC (consulting firm); Chief Investment Officer of Knights of Columbus (fraternal benefit society selling life insurance and annuities).	1	Lead Trustee, Third Avenue Funds (fund complex consisting of five funds and one variable series trust).
<b>OFFICERS</b>					
Andrew Dakos*** (45)	President as of October 2009.	1 year; Since 2009	Principal and Chief Compliance Officer of the Adviser; Principal of the general partner of several private investment partnerships in the Bulldog Investors group of funds.	n/a	n/a
Rajeev Das (42)	Vice-President and Treasurer as of October 2009.	1 year; Since 2009	Principal, Bulldog Investors, a group of Investment Funds; Managing member of the General Partner of Opportunity Income Plus L.P., an investment fund.	n/a	n/a

# Special Opportunities Fund, Inc.

## Supplemental information (unaudited)

<b>Name, Address and Age*</b>	<b>Position(s) Held with the Fund</b>	<b>Term of Office and Length of Time Served</b>	<b>Principal Occupation During the Past Five Years</b>	<b>Number of Portfolios in Fund Complex Overseen by Director**</b>	<b>Other Directorships held by Director</b>
Phillip Goldstein*** (66)	Chairman and Secretary as of October 2009.	1 year; Since 2009	Principal of the Adviser; Principal of the general partner of several private investment partnerships in the Bulldog Investors group of funds.	n/a	n/a
Gerald Hellerman**** (74)	Chief Compliance Officer and Chief Financial Officer as of January 2010.	1 year; Since 2009	Managing Director of Hellerman Associates (a financial and corporate consulting firm).	n/a	n/a

\* The address for all directors and officers is c/o Special Opportunities Fund, Inc., 615 East Michigan Street, Milwaukee, WI 53202.

\*\* The Fund Complex is comprised of only the Fund.

\*\*\* Messrs. Dakos and Goldstein are each considered an "interested person" of the Fund within the meaning of the 1940 Act because of their affiliation with Brooklyn Capital Management, LLC, the Adviser and their positions as officers of the Fund.

\*\*\*\* Mr. Hellerman is considered an "interested person" of the Fund within the meaning of the 1940 Act because he serves as the Fund's Chief Compliance Officer and Chief Financial Officer. Mr. Hellerman is not affiliated with Brooklyn Capital Management, LLC.

# Special Opportunities Fund, Inc.

## New York Stock Exchange certifications (unaudited)

On January 4, 2012, the Fund submitted an annual certification to the New York Stock Exchange (“NYSE”) in which the Fund’s president certified that he was not aware, as of the date of the certification, of any violation by the Fund of the NYSE’s Corporate Governance listing standards. In addition, as required by Section 302 of the Sarbanes-Oxley Act of 2002 and related SEC rules, the Fund’s president and treasurer have made quarterly certifications, included in the filing with the SEC on Forms N-CSR and N-Q, relating to, among other things, the Fund’s disclosure controls and procedures and internal control over financial reporting.

# Special Opportunities Fund, Inc.

## Privacy policy notice

The following is a description of the Fund's policies regarding disclosure of nonpublic personal information that you provide to the Fund or that the Fund collects from other sources. In the event that you hold shares of the Fund through a broker-dealer or other financial intermediary, the privacy policy of the financial intermediary would govern how your nonpublic personal information would be shared with unaffiliated third parties.

**CATEGORIES OF INFORMATION THE FUND COLLECTS.** The Fund collects the following nonpublic personal information about you:

1. Information from the Consumer: this category includes information the Fund receives from you on or in applications or other forms, correspondence, or conversations (such as your name, address, phone number, social security number, assets, income and date of birth); and
2. Information about the Consumer's transactions: this category includes information about your transactions with the Fund, its affiliates, or others (such as your account number and balance, payment history, parties to transactions, cost basis information, and other financial information).

**CATEGORIES OF INFORMATION THE FUND DISCLOSES.** The Fund does not disclose any nonpublic personal information about their current or former shareholders to unaffiliated third parties, except as required or permitted by law. The Fund is permitted by law to disclose all of the information it collects, as described above, to its service providers (such as the Custodian, administrator and transfer agent) to process your transactions and otherwise provide services to you.

**CONFIDENTIALITY AND SECURITY.** The Fund restricts access to your nonpublic personal information to those persons who require such information to provide products or services to you. The Fund maintains physical, electronic and procedural safeguards that comply with federal standards to guard your nonpublic personal information.

**This privacy policy notice is not a part of the shareholder report.**

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**Investment Adviser**

Brooklyn Capital Management, LLC  
Park 80 West  
250 Pehle Avenue, Suite 708  
Saddle Brook, NJ 07663

**Administrator and Fund Accountant**

U.S. Bancorp Fund Services, LLC  
615 East Michigan Street  
Milwaukee, WI 53202

**Custodian**

U.S. Bank, N.A.  
Custody Operations  
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Milwaukee, WI 53212

**Transfer Agent and Registrar**

American Stock Transfer & Trust Company, LLC  
59 Maiden Lane  
New York, NY 10038

**Independent Registered Public Accounting Firm**

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**Special Opportunities Fund, Inc.**

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