

January 20, 2006

Paul J. Schroeder, Jr.  
General Counsel  
Dillard's Inc.  
1600 Cantrell Road  
Little Rock, AR 72201

Dear Mr. Schroeder:

Several years have passed since we last had a substantive discussion about Dillard's apparel sourcing standards. We would like to request a meeting with you to learn about what has transpired at the company since that time and what steps the company has taken to better identify, assess and control for sourcing risks. Overlooking these risks can have a serious impact on brand, reputation, and ultimately, shareholder value.

As this letter will detail, much progress has been made on global labor standards in the retail industry over the past few years in terms of monitoring, reporting, and implementation. As investors with nearly 587,000 shares of Dillard's, we would like to again engage in a thoughtful discussion of these important issues and learn about Dillard's approach to keep pace with its competitors.

While Dillard's has a code of conduct, purchase order requirements, and incorporates two of the ILO conventions, we believe that introducing independent monitoring, adding ILO conventions, and becoming more transparent can help the company to increase its competitiveness, reduce risk, and enhance the credibility of its existing supplier code of conduct.

As you are aware, for the past four years shareholders have repeatedly requested a report from the company about its sourcing practices and programs. This type of transparency is an important aspect of corporate social responsibility and is a critical tool for building trust with investors and the public. While we do have information that the company provided to us some years back, we would like to receive an update about changes and enhancements to and implementation and monitoring of its policies so that we may gain a more informed opinion about the company's performance in this area.

I hope you will agree to meet or have a conference call so that we can update each other about the latest happenings in global labor standards. Please let me know at your earliest convenience a time and date that would be suitable for our discussion. You can reach me at 212-503-1947. Feel free to call as well with any questions or if you would like additional information about the issues we have raised. We look forward to hearing from you.

Thank you for your attention to our concerns.

Sincerely,

Julie B. Tanner  
Corporate Advocacy Coordinator  
Christian Brothers Investment Services

Julie Gozan  
Director of Corporate Governance  
Amalgamated Bank

Don Kirshbaum  
Investment Officer – Policy  
State of Connecticut  
Office of the Treasurer

Rev. David Schilling  
Program Director  
Global Corporate Accountability Program  
The Interfaith Center on Corporate Accountability

Patrick Doherty  
Office of the Comptroller  
City of New York

CC: Board of Directors

William Dillard, II, Director; Chief Executive Officer  
Alex Dillard, Director; President  
Mike Dillard, Director; Executive Vice President  
Drue Corbusier, Director; Executive Vice President  
James I. Freeman, Director; Senior Vice President, Chief Financial Officer  
Robert C. Connor, Director  
Will D. Davis, Director  
John Paul Hammerschmidt, Director  
Peter R. Johnson, Director  
Warren A. Stephens, Director  
William H. Sutton, Director  
J.C. Watts, Jr., Director

## COMPETITOR PROGRESS

### A. Disclosure

1. Disclosing Policies and Codes: **Apparel manufacturers and retailers such as The Gap, Nike, Nordstrom, Jones Apparel Group, Kohl's, J. C. Penney, Sears, Kellwood, VF, Wal-Mart, Federated Department Stores and May Department Stores (now merged), and Hudson's Bay Company** have recognized the growing relevance of global labor standards practices and have disclosed their supplier codes of conduct in publicly available reports.

Transparency is an important aspect of corporate social responsibility and is a critical tool for building trust with investors and the public. While Dillard's makes its code of conduct available upon request, several of Dillard's competitors noted above disclose their supplier codes to the public. This presents an opportunity for Dillard's to join the list of companies that are demonstrating best practice in the industry and publicly release its policy. One suggestion could be to place the company's supplier code on the webpage that includes Dillard's various codes of conduct:  
<http://www.shareholder.com/dillards/conduct.cfm>

2. Providing Information on Implementation and Monitoring Systems Mechanisms: In addition to disclosing policies and Codes, companies should periodically disclose information about the implementation and monitoring of its policies in order to permit their stakeholders to gain a more informed opinion about corporate performance in this area. Over time, this information should allow companies to establish an easily understood track record, to more effectively measure its own performance against its stated policies, and to describe progress that will or has been achieved in addressing global supplier standards.

Being transparent and detailing codes and policies can also help the company gain credibility in the eyes of its stakeholders. While Dillard's states that it has incorporated labor and human rights requirements into purchase contracts and buying agreements and has engaged in limited monitoring of suppliers' factories, evidence has not been provided. We would recommend that Dillard's provide this type of information in a corporate responsibility or supplier standard report, omitting confidential data. This is needed for investors to compare which companies are implementing robust programs of supply chain monitoring and which are not. We hope that Dillard's will join with the increasing number of companies that routinely provide and update this type of information for shareholders, stakeholders and the public.

3. Reporting to Stakeholders: Responding to interest from customers, stockowners, and other stakeholders about company policies and programs to address supply chain issues, many companies are describing their initiatives in corporate social responsibility (CSR). Over 1500 companies in the world issued sustainability or environmental reports in 2004, including almost half (49) of the 100 largest companies in the world. **The Gap, Nike, Hudson's Bay and Wal-Mart** have also issued supplier standard reports detailing their policies, practices and programs.

Examples:

**The Gap:** In 2004, the company released its first corporate social responsibility report, detailing working conditions in over 300 factories that make its clothing. The Gap collaborated with a number of research, labor and monitoring organizations to document workplace practices in non-U.S. plants. In its report, the company publicly disclosed its factory rating system and published a broad sample of scores. It is considered to be one of the most transparent and comprehensive public reports on supplier compliance programs. Although the report represented one-tenth of Gap suppliers and found that many of them failed

core labor standards, socially responsible shareholders were impressed with the company's honest assessment, its disclosure, and its commitment to future improvements.

**Nike:** Nike's 2004 Corporate Responsibility report contains disclosure of its supplier factory locations, listing 700 contract factories worldwide, and provides detailed information on code of conduct non-compliance. We believe this report is in keeping with the current trend within the apparel industry toward improved supply chain transparency.

**Wal-Mart:** Wal-Mart has published a Supplier Standards public report for four years. In 2004 Wal-Mart made public its 2004 Report, which contains more information on its monitoring, process of remediation, and areas of concern than previous reports. ICCR members provided substantial feedback to two drafts before the company finalized this report.

## **B. Strengthening Policies and Codes**

1. Incorporating ILO Conventions: Several of Dillard's competitors have adopted more than 2 conventions, including: **Kellwood, Kohl's, VF, Nordstrom, Federated/May Department Stores**, and Wal-Mart. The ILO conventions are global standards that are a matter of international law. While Dillard's upholds two ILO standards -- no use of child or forced labor, including bonded or prison labor -- we would strongly recommend that Dillard's update its policy to include the right of workers to form and join trade unions, to bargain collectively, to not be subject to discrimination or intimidation, and to have equal opportunity regardless of race, color, sex, religion, political opinion, age, nationality, social origin, or other distinguishing characteristics. Adhering to two aspects of ILO conventions is limiting in that each convention is designed to protect a fundamental area of workers rights.

In a review of supplier and labor issues conducted by IRRC in 2004, it found that eight of forty retail firms guaranteed workers freedom of association, while five guaranteed workers the right to organize and bargain collectively, falling in line with ILO conventions 87 and 98. Fourteen tackled discrimination, with five guaranteeing equal pay for equal work and complying with ILO convention 100. **Kohl's** included all of the classifications in ILO convention 111.

2. Instituting Independent Monitoring: We believe that Dillard's policy would be more credible if it were strengthened to include independent monitoring of corporate adherence to these internationally recognized principles. For our company's commitment to human rights to be maintained, we would strongly urge the company to commit to independent monitoring, which can lead to robust and effective management of supply chain issues while diminishing the potential for breakdowns in the system, such as labor strife, negative publicity, lawsuits or fines.

While Dillard's has stated in its proxy materials that independent monitoring can put undue financial burdens on the company without evidence of problems, shareholders believe that a proactive company like Dillard's, with more than 300 stores, would not wait for controversies to arise before taking action to protect the company's reputation. For example, a report by a non-profit group issued in March 2005 cited Dillard's as one of several companies using a factory in Thailand that allegedly forces overtime and pays by the piece instead of offering minimum wage.

ICCR members would recommend that Dillard's involve non-governmental organizations in monitoring, including local organizations with experience in tracking labor and human rights issues. NGOs can also make good partners since they could be seen as being independent of the company and therefore could engender the trust of workers to report any abuses that have occurred without fear of punishment or retribution.

### **C. Costs and Benefits**

While there are costs associated with translating codes and policies, training personnel, communicating new policies with staff, and developing monitoring mechanisms, we believe these elements can help Dillard's to reduce risks now and in the long run. They can also work to protect the company's overall image and brands and potentially reduce negative publicity, consumer boycotts, or lawsuits.

#### **Questions for discussion**

The last policy that we had received from the company is from 1996. Is there an updated version or have any elements been added or changed?

The company notes that it has provided copies of the policy to interested shareholders on request. Is Dillard's considering making this material publicly available? If not, why?

It is stated that Dillard's employees personally inspect select factories to verify compliance. How often, how many, and what are the findings? While we believe that internal monitoring is essential, it is not a substitute for external monitoring. For example, in many cases workers cannot candidly report to internal monitors.

It is our understanding that Dillard's reserves the right to break contracts with vendors who violate human rights. Is this in the contract with their suppliers? What are the specific grounds for termination? Have contracts been broken?

Regarding breaking contracts for human rights violations, what type of human rights monitoring does the company conduct? How does Dillard's avoid a conflict of interest since it is the buying agents that recommend factories yet it is to advise the company that factories it selected are violating human rights?

We have noted that Dillard's buying agents must report violations to the company and are required to periodically inspect factories to ensure compliance with the standards. Have violations been reported, and what steps have been taken? Is there the potential for a conflict of interest to get this information from buying agents, and not through outside verification?

How has Dillard's addressed the report from March 2005 that mentioned the company as one of several companies using a factory in Thailand that allegedly forces overtime and pays by the piece instead of offering minimum wage?