



CHARTWELL TECHNOLOGY INC.

**Management's Discussion and Analysis of Financial Condition and Results of Operations
for the three and nine months ended July 31, 2006 and 2005.**

September 13, 2006

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") should be read in conjunction with Chartwell Technology Inc.'s ("Chartwell" or the "Company") audited consolidated financial statements and the accompanying notes for the year ended October 31, 2005, which have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP"). Additional information relating to the Company is available on SEDAR at www.sedar.com under Chartwell Technology Inc. and on the Company's website at www.chartwelltechnology.com.

Special Note Regarding Forward-Looking Statements

This MD&A contains certain forward-looking statements which reflect Management's expectations regarding the Company's growth, results of operations, performance and business prospects and opportunities.

Statements about the Company's future plans and intentions, results, levels of activity, performance or achievements or other future events constitute forward-looking statements. Where possible, words such as "anticipate", "estimate", "may", "will", "should", "could", "expect", "plan", "intend", "believe", "estimate", or "potential" or similar words, have been used to identify these forward-looking statements.

Forward-looking statements involve significant risks, uncertainties and assumptions. Many factors could cause actual results to differ materially from the results discussed or implied in the forward-looking statements. These factors should be considered carefully and readers should not place undue reliance on the forward-looking statements.

Factors which could cause results or events to differ from current expectations include, among other things: the impact of government regulation and laws affecting international operations; the impact of price competition; the ability of the Company to retain and attract qualified professionals; the impact of rapid technological and market change; loss of business or credit risk with current and prospective major customers; general industry and market conditions and growth rates; currency rate fluctuations and the impact of consolidations in the on-line gaming industry. Further information is provided under the heading "Risks and Uncertainties" in this MD&A, which readers are encouraged to review. Chartwell disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except as required by law. No assurance can be given that actual results, performance or achievement expressed in, or implied by, forward-looking statements within this disclosure will occur, or if they do, that any benefits may be derived from them.

Past performance has been considered in drawing conclusions with respect to forward-looking statements contained in this MD&A.

EBITDA is defined as earnings before interest, taxes, depreciation and amortization. EBITDA is not a recognized measure under Canadian generally accepted accounting principles. Management believes however that EBITDA is a useful supplementary measure as it provides indication of the results of Chartwell's business operations without regard to how these activities were financed or how these results were taxed. Chartwell's method of calculating EBITDA may differ from that of other companies, and accordingly, EBITDA may not be directly comparable to measures used by other companies.

OVERVIEW

Chartwell develops, markets, licenses, implements and supports gaming applications and entertainment content for the internet and wireless platforms. Chartwell's JAVA and Flash based software products and games are designed for deployment in gaming, entertainment and promotional applications. Chartwell does not operate a gaming site nor do we operate our clients' gaming sites.

Business Plan

The Company's business plan and objectives through fiscal 2006 are: to increase our market share in the traditional internet casino market, with a continued emphasis on the European market; further develop the liquidity of our poker community; establish liquidity in our bingo community; commercially release our Flash poker product and further develop poker variants and establish market share in these new market areas. We will continue to focus on product development and diversification of our products, customers and revenues.

Business Model

The majority of Chartwell's revenue is in the form of software license fees. License fees, including fees from master license agreements, most of which are contingent upon customer usage, are recognized on an accrual basis as earned over the life of the contract. Licensees pay an ongoing fee for the licensing and support of the Company's software under a software licensing agreement, which typically has a three to five year term. The license fee is calculated as a percentage of each licensee's level of activity. Additional revenue is derived from software set-up fees and software development fees. Software set-up fees are one time fees for new customer development and installations. The Company's contractual agreements with licensees provide for the provision of graphics, web design, software implementation services, licensing of the software and provision of software upgrades over the term of the contract. Set-up fee revenue and related costs are recognized ratably over the term of the contract. Software development fees are fees that the Company charges for software development services relating to software programming services. These fees are recognized on a percentage-of-completion basis and reported in other revenue.

Expenses are classified into six categories, namely: software development and support; sales and marketing; general and administrative ("G&A"); depreciation and amortization, stock-based compensation expense and foreign currency gains or losses. Software development and support consists of personnel and related costs associated with the design and development of new products, support of existing products, hosting costs for the poker community paid to hosting provider, customer implementation and quality assurance. Sales and marketing expenses consist of personnel and related costs associated with the Company's sales, marketing and business development activities. G&A expenses include the costs of all administrative, financial and IT personnel, investor relations and professional fees relating to our public company listing. Stock-based compensation expense consists of the estimated fair value of options granted to employees and consultants. Depreciation and amortization are based on the estimated useful life of our assets and include the amortization of deferred software development costs and the intangible assets acquired as part of the acquisition of Micropower Corporation Limited ("Micropower"). The Company operates internationally with 100% of its revenue derived from non-Canadian licensees. Under the Company's licensing agreements, the majority of the Company's revenue is received in Euros and U.S. dollars. Consequently, the Company is exposed to currency fluctuations, which result in foreign currency gains or losses, which are reported in this expense category.

HIGHLIGHTS

Chartwell reported its sixteenth consecutive quarter of profitability in the three months ended July 31, 2006.

Total revenue increased to \$4.7 million and \$13.9 million for the three and nine months ended July 31, 2006, respectively, as compared to \$4.5 million and \$13.2 million for the three and nine months ended July 31, 2005, respectively. During the quarter, an increase in Chartwell's revenue from new business and growth in revenue from existing customers was offset by declines in revenue from customers with exposure to the Italian market. As a result of controversial legislation introduced by the Italian government, access to the Italian market by certain number of Chartwell's customers has been limited. European Union authorities are investigating these actions of the Italian government. Net income decreased to \$0.5 million and \$1.1 million, respectively, for the three and nine months ended July 31, 2006 respectively, compared to \$0.7 million and \$3.1 million for the comparative periods of 2005 with diluted earnings per share of \$0.03 and \$0.06 for the three and nine months ended July 31, 2006 respectively, compared to \$0.04 and \$0.16 for the comparative periods of 2005. Chartwell has grown significantly in size of personnel from the same periods in 2005. The Company continues to invest in developing our products to meet requirements under new customer agreements that will take effect in the near future. In addition, net earnings for the nine months ended July 31, 2006 were adversely affected by a \$1.0 million provision for a doubtful account, relating to one customer in the second quarter of 2006.

During fiscal 2006, the Company continues to invest in key areas of its business specifically related to product development and support and sales and marketing. To sustain and build for long term growth it is expected that the Company will maintain its current level of expenditures throughout the remainder of the fiscal 2006.

Chartwell maintains a strong balance sheet. At July 31, 2006, the Company had cash and short-term investments of \$15.2 million, working capital (defined as current assets less current liabilities) of \$18.2 million and no debt.

Chartwell's internal control systems continue to evolve as the Company grows. We believe these systems are sufficient to execute our business plan and to provide meaningful information upon which to manage our business. Management believes that the disclosure controls and procedures that are currently in place are effective.

SUMMARY OF FINANCIAL RESULTS

Comparative Quarterly Operating Results (in thousands, except share data)

The following table sets out selected unaudited financial information of the Company on a consolidated basis for the last eight quarters.

	Q3 2006	Q2 2006	Q1 2006	Q4 2005	Q3 2005	Q2 2005	Q1 2005	Q4 2004
Revenue								
Software license fees	\$ 4,383	\$ 4,449	\$ 4,275	\$ 4,113	\$ 4,028	\$ 3,630	\$ 4,622	\$ 3,237
Software set-up fees	69	65	51	69	348	125	115	208
Interest & other	211	243	115	467	132	122	78	44
	<u>4,663</u>	<u>4,757</u>	<u>4,441</u>	<u>4,649</u>	<u>4,508</u>	<u>3,877</u>	<u>4,815</u>	<u>3,489</u>
Expenses								
Software development & support	2,141	1,740	1,795	1,639	1,754	1,319	1,325	1,238
Sales & marketing	566	545	580	555	488	551	650	303
General & administrative	841	1,650	548	522	418	227	408	657
Amortization of intangible assets	123	123	123	86	19	-	-	-
Amortization of deferred software development costs	59	59	59	58	59	59	59	59
Stock-based compensation	89	171	224	230	198	91	118	103
Depreciation & amortization	114	100	95	102	54	68	36	53
Foreign currency loss (gain)	(68)	45	132	72	338	(15)	(20)	247
	<u>3,865</u>	<u>4,433</u>	<u>3,555</u>	<u>3,264</u>	<u>3,328</u>	<u>2,300</u>	<u>2,576</u>	<u>2,660</u>
Net income before taxes	798	324	886	1,384	1,180	1,577	2,239	829
Income taxes	322	223	382	534	452	643	753	(631)
Net Income	<u>\$ 476</u>	<u>\$ 101</u>	<u>\$ 504</u>	<u>\$ 850</u>	<u>\$ 728</u>	<u>\$ 934</u>	<u>\$ 1,486</u>	<u>\$ 1,460</u>
Basic earnings per share	0.03	0.01	\$ 0.03	\$ 0.04	\$ 0.04	\$ 0.05	\$ 0.09	\$ 0.10
Diluted earnings per share	0.03	0.01	\$ 0.03	\$ 0.04	\$ 0.04	\$ 0.05	\$ 0.08	\$ 0.08

QUARTERLY RESULTS

FOR THE THREE AND NINE MONTHS ENDED JULY 31, 2006 COMPARED TO THE THREE AND NINE MONTHS ENDED JULY 31, 2005 (all amounts rounded in Canadian dollars except where noted).

REVENUE

In the three and nine months ended July 31, 2006, total revenue increased by 3.4% and 5.0% to \$4.7 million and \$13.9 million, respectively, compared to \$4.5 million and \$13.2 million in the same period of 2005. During the quarter, a near 30% increase in Chartwell's revenue from new business and growth in revenue from existing customers was offset by declines in revenue from customers with exposure to the Italian market. As a result of controversial legislation introduced by the Italian government, access to the Italian market by a certain number of Chartwell's customers has been severely limited. The European Union authorities are investigating these actions.

Software license fees increased by 8.8% and 6.7% to \$4.4 million and \$13.1 million for the three and nine months ended July 31, 2006 respectively, from \$4.0 million and \$12.3 million in the same periods of 2005. The net increase in license fees reflects the impact of clients that began contributing to revenue in early fiscal 2006 and increased volumes in the poker community, offset a decrease in revenues primarily from customers with exposure to the Italian market.

Software set-up fees decreased to \$70,000 and \$185,000 from \$348,000 and \$587,000 for the three and nine months ended July 31, 2006 and 2005, respectively. Software set-up fees, as a percentage of total revenue, decreased to 1.5% and 1.3% from 7.7% and 4.5% for the three and nine months ended July 31, 2006 and 2005, respectively. This is due to lower set-up fees from new clients and often, due to their nature, reflects volatility over time. In addition, there were incremental software set-up and development fees recognized for the three months ended July 31, 2005 representing certain non-material amounts related to the recognition of deferred revenue on contracts that were terminated in the quarter. These amounts did not recur for the similar period of 2006. We expect that software set-up fees will continue to represent a small percentage of the Company's sales revenue as we continue to build our license fee component of revenue.

Interest and other income increased to \$211,000 and \$569,000 in the three and nine months ended July 31, 2006, compared to \$132,000 and \$333,000 for the same period of 2005. The increase is attributable to the Company earning higher rates of interest on cash and short term investments.

Operating Expenses

Total operating expenses, including foreign exchange gains and losses and net of deferred software development costs, increased by 16.2% and 44.5% to \$3.9 million and \$11.9 million for the three and nine months ended July 31, 2006 respectively, as compared to \$3.3 million and \$8.2 million for the same periods of 2005. The increase in operating expenses is reflective of the Company's growth in personnel and supporting infrastructure. In addition to higher expenses relating to software development and support, the Company incurred higher expenses in the areas of stock-based compensation as well as depreciation and amortization resulting from the intangible assets acquired in the acquisition of Micropower. Increases in general and administration costs resulting from the Company's larger scale and administrative requirements also contributed to the increased operating expenses. In addition, an allowance for a doubtful account of \$1.0 million was recorded to general and administrative expenses in the second quarter of 2006 causing an increase in the year-to-date operating expenses.

SOFTWARE DEVELOPMENT & SUPPORT

Software development and support expenses, net of deferred software development costs, increased by 22.1% and 29.0% to \$2.1 million and \$5.7 million for the three and nine months ended July 31, 2006 respectively, compared to \$1.8 million and \$4.4 million for the same periods of 2005. Salaries and consulting fees continue to represent the largest expenditure area and accounted for 62.7% and 68.7% of total software development and support costs for the three and nine months ended July 31, 2006, respectively. The increased levels of expenditure represent higher headcount and costs associated with increased traffic within the poker community. Software development and support costs are net of deferred development costs related to the poker community as well as the mobile product which were \$736,000 and \$1.8 million for the three and nine months ended July 31, 2006, compared to deferred development cost reductions for the poker community which were \$190,000 and \$268,000 for the same periods in 2005. Given the increased deferrals for poker and mobile, the magnitude of the increase to software development and support expense lessened.

As a percentage of revenue, software development and support expenses, net of deferred software development costs, were 45.9% and 38.9% for the three and nine months ended July 31, 2006, respectively. These percentages have increased over the comparative periods of 2005, which were 38.9% and 33.3%, representing the effect of the above increases. Software development and support expenses are increasing in line with the Company's growth strategies.

GENERAL AND ADMINISTRATIVE

G&A expenses increased to \$0.8 million and \$3.0 million from \$0.4 million and \$1.1 million for the three and nine months ended July 31, 2006 respectively, compared to the same periods of 2005. Contributing to the increase for the nine month comparative periods is additional infrastructure costs required to support the growth in personnel, including higher facility costs, higher legal and regulatory fees, higher professional fees due to the establishment and expansion of operations in Malta and related corporate structure planning, and increased investor relations activities. The single largest year-over-year increase for the nine months ended July 31, 2006 is due to a \$1.0 million expense related to an allowance for a doubtful account recorded in the second quarter of 2006 versus a bad debt expense recovery of \$132,000 recorded in the second quarter of 2005.

As a percentage of revenue, G&A expenses increased to 18.0% for the three months ended July 31, 2006 from 9.3% for the three months ended July 31, 2005, respectively. This percentage increased due the overall increase in infrastructure costs which do not grow proportional with revenue growth. This percentage is expected to remain consistent for the remainder of the year.

SALES AND MARKETING

Sales and marketing expenses increased to \$0.6 million and \$1.7 million for the three and nine months ended July 31, 2006, respectively, from \$0.5 million and \$1.6 million for the same period of 2005. The increase is primarily attributable to increased costs related to promotions within the poker community to stimulate poker business and increased trade show and travel costs over the comparative periods. Chartwell will continue to invest in promotion of the poker community throughout fiscal 2006.

As a percentage of revenue, sales and marketing expenses decreased to 12.1% and 12.2% from 10.8% and 12.4% for the three months and nine months ended July 31, 2006 and 2005, respectively. This rate is expected to continue for the remainder of the fiscal year.

AMORTIZATION OF INTANGIBLE ASSETS

Amortization of intangible assets is related to amortization of the customer contracts and intellectual property acquired through the acquisition of Micropower. The expenses for the three and nine months ended July 31, 2006 are \$123,000 and \$370,000, with comparative expenses of \$19,000 and \$19,000 for the three and nine months ended July 31, 2005, respectively. The value recorded for customer contracts is being amortized over the contract period for each acquired contract (i.e. as cash flows are being generated for Chartwell). The value recorded for intellectual property is being amortized over five years, which is Management's best estimate of the time period that the acquired intellectual property will provide future value to Chartwell.

AMORTIZATION OF DEFERRED SOFTWARE DEVELOPMENT COSTS

Amortization of deferred software development costs for the three and nine months ended July 31, 2006 were \$59,000 and \$176,000, respectively, compared to \$59,000 and \$176,000 for the same periods in 2005. In fiscal 2003 and fiscal 2004, the Company deferred \$531,000 and \$175,000, respectively, of software development costs relating to the development of the Company's community poker product. Management has estimated that the appropriate amortization period would be three years. The Company began amortizing these costs on a straight line basis in the third quarter of fiscal 2004. In fiscal 2005 and the first three quarters of fiscal 2006, the Company deferred an additional \$2.1 million of software development costs related to the development of version 2.0 of the Company's community poker product, which builds on the intellectual property acquired in the acquisition of Micropower. In the second and third quarters of 2006, the Company deferred \$364,000 of software development costs related to the development of the Company's mobile product. The costs for the community poker and mobile products have not been amortized to date, given that these versions of the products have not yet been launched.

STOCK-BASED COMPENSATION

The Company recorded \$89,000 and \$484,000 of stock-based compensation expense for the three and nine months ended July 31, 2006, compared to \$198,000 and \$406,000 for the three and nine months ended July 31, 2005. Stock-based compensation expense relates to the amortization of the fair value of stock options granted to employees, directors and consultants. Stock based compensation is amortized over the applicable vesting period ranging from three to five years. The year over year decrease in this expense is due to fewer options issued and a higher level of option exercise and expiries, thus decreasing the number of options outstanding.

DEPRECIATION & AMORTIZATION

Depreciation and amortization increased to \$114,000 and \$309,000 for the three and nine months ended July 31, 2006, compared to \$54,000 and \$158,000 for the same period of 2005. The increase in depreciation is due to higher net book values of property and equipment at July 31, 2006 compared to July 31, 2005. Significant hardware was acquired in the fourth quarter of 2005 and the first quarter of 2006 to integrate the Micropower staff into the Chartwell environment and to build up their infrastructure. In the second and third quarters of 2006, additional investments were made in computer equipment including servers to handle additional volumes as well as computer equipment upgrades and office furniture to accommodate the Company's growth. It is expected that continued investment in computer hardware and software will be required as the Company continues to grow.

FOREIGN CURRENCY GAIN/LOSS

The Company experienced a foreign currency gain of \$69,000 for the three months ended July 31, 2006 and a foreign currency loss of \$108,000 for the nine months ended July 31, 2006 respectively, compared to foreign currency losses of \$338,000 and \$303,000 for the comparative periods of 2005. The foreign currency gain experienced in the third quarter of 2006 was due to lower foreign currency denominated accounts receivable balances and more favorable foreign exchange rates during the third quarter of 2006 compared to the same period of 2005. The Company does not utilize hedges or forward contracts to mitigate foreign currency risk.

PROVISION FOR INCOME TAXES

Income taxes for the three and nine months ended July 31, 2006 decreased to \$322,000 and \$927,000 compared to \$452,000 and \$1.8 million for the comparative period of 2005. The reduction in tax expense is attributable to the lower level of pre-tax income.

EBITDA

EBITDA (defined as net income less interest, plus taxes, depreciation and amortization) decreased to \$883,000 from \$1.2 million for the three months ended July 31, 2006 and 2005, respectively. The change in EBITDA between the two periods is due to increased revenues, offset by higher expenses in 2006. EBITDA decreased to \$2.3 million from \$5.0 million for the nine months ended July 31, 2006 and 2005, respectively. The decrease in EBITDA is primarily due to higher levels of expenses, including a significant provision for a doubtful receivable made in the second quarter of 2006.

Net Income

Net income decreased by 34.7% and 65.7% to \$0.5 million and \$1.1 million for the three and nine months ended July 31, 2006, versus \$0.7 million and \$3.1 million for the three and nine months ended July 31, 2005. The decrease in net income for the first three quarters of 2006 compared to the similar period of 2005 is primarily due to higher levels of expenses, including a significant provision for a doubtful receivable made in the second quarter.

Diluted earnings per share were \$0.03 and \$0.06 for the three and nine month periods ended July 31, 2006, compared to \$0.04 and \$0.16 in the same periods of 2005.

Liquidity and Capital Resources

Operating Activities

Cash generated from operating activities for the three and nine months ended July 31, 2006 was \$1.8 million and \$1.9 million, respectively, compared to (\$82,000) and \$2.9 million for the three and nine months ended July 31, 2005. The increase in the three month comparative periods was primarily due to lower levels of accounts receivable. The decline of \$1.0 million between the nine month comparative periods was due to lower levels of accounts receivable offset by significant income tax payments.

Financing Activities

Cash flows used in financing activities were \$1.3 million and \$3.4 million for the three and nine months ended July 31, 2006, respectively, versus cash flows provided by financing activities of \$341,000 and \$11.2 million for the three and nine months ended July 31, 2005. The Company's financing activities in the third quarter of 2006 consisted primarily of the issuance of shares for cash resulting from the exercise of stock options, offset by cash used to repurchase 443,600 shares under the Normal Course Issuer Bid ("NCIB"). The Company has repurchased a total of 932,100 shares under the NCIB. In addition to these activities, in the nine months ended July 31, 2006, cash was used to repay the amount due to Honeycomb Holdings Limited, which was recorded on the acquisition of Micropower. The change from the nine months ended July 31, 2005 was due to the private placement financing completed in the first quarter of 2005, for net cash proceeds of \$10.5 million. As well, the Normal Course Issuer Bid was not in effect in 2005 therefore there were no comparative cash payments.

Investing Activities

Cash flows provided by investing activities were \$254,000 and \$2.7 million for the three and nine months ended July 31, 2006, respectively, versus cash flows provided by investing activities of \$737,000 and used by investing activities of \$16.1 million for the three and nine months ended July 31, 2005, respectively. The Company's investing activities in the three and nine months ended July 31, 2006 consisted mainly of the redemption of short term investments, deferred development costs and the purchase of property and equipment, which include computers and software. The change from the three and nine months ended July 31, 2005 was due to the purchase of \$12.6 million in short term investments in 2005 in order to invest cash received from a private placement financing. Also, a deposit was paid on the Micropower acquisition in the first quarter of 2005, with no comparative payment made in 2006.

Contractual Obligations

The Company's future minimum annual payments under operating and capital leases are the following:

2006	\$159,080
2007	593,736
2008	544,989
2009	510,770
Thereafter	41,994

Related Party Transactions

Software development and support expenses for the three months ended July 31, 2006 include legal fees of \$69,000 and consulting fees of \$41,000 paid to certain officers of the Company in the normal course of business. For the nine months ended July 31, 2006, the Company incurred legal fees \$215,000 and consulting fees of \$124,000 to certain officers and directors of company in the normal course of business. As at July 31, 2006, \$66,000 is recorded to accounts payable and accrued liabilities, while all other amounts have been paid. Amount due from related party of \$165,000 is an amount due from a Company officer. The amount due bears 6% interest, is secured by 189,000 common shares of the Company and has no set terms of repayment.

Accounting Policies and Estimates

Critical accounting policies and methods used in the preparation of the Company's financial statements are described in note 1 to the consolidated financial statements of the Company for the year ended October 31, 2005. There have been no changes to critical accounting policies in the three month period ended July 31, 2006.

Risks and Uncertainties

General

The Company and its subsidiaries operate in a rapidly changing environment that involves numerous risks and uncertainties, many of which are beyond our control and which could have a material effect on our business, revenue, operating results and financial condition. The following highlights some of these risks and uncertainties.

Government Regulation/International Operations

The Company and our software licensees are subject to applicable laws and regulations in the jurisdictions in which they operate, such as Belize, Malta, Gibraltar, Netherlands Antilles and others. The majority of the Company's revenue is derived from software license fees in countries outside North America. Some jurisdictions have introduced legislation and rules attempting to restrict or prohibit online gaming, while other jurisdictions have taken the position that online gaming is legal and have adopted (or are in the process of considering) legislation to regulate online gaming. There are burdens and uncertainties associated with operating in these jurisdictions, including complying with multiple and sometimes conflicting regulatory and legal requirements and interpretations, potential restrictions on gaming activities and potentially adverse tax risks, any of which could have a material adverse effect on the Company's revenue, results of operations and financial condition.

The UK intends to establish a regulated market for online gaming. The Isle of Man and Alderney, both in the British Isles, are already regulated environments for Internet gaming, based on standards consistent with land-based gaming. The British government has enacted legislation to create a regulated and licensed jurisdiction for Internet gaming. Compliance with that legislation may result in increased costs that could have a material adverse effect on the Company's revenue, results of operations and financial condition.

Existing legislation in some jurisdictions, including US federal and state statutes, has been and could continue to be construed to prohibit or restrict gaming through the use of the Internet and there is a risk that governmental authorities may view the Company and/or our licensees as having violated such statutes. Therefore, there is a risk that legal proceedings could be initiated against us, our licensees, Internet Service Providers ("ISPs") and others involved in the Internet gaming industry. This could potentially result in our incurring substantial litigation and legal expenses, penalties, fines, injunctions or other remedies or restrictions being imposed upon us or our licensees while diverting the attention of Management. Such proceedings could have a material adverse effect on the Company's revenue, results of operations and financial condition.

As companies and consumers involved in online gaming, including our licensees and their players, are located in different jurisdictions around the world, there is uncertainty regarding the future regulatory framework for online gaming. There is a risk that proposed legislation supporting online gaming may not be passed and that existing legislation supporting online gaming may be changed. Changes to the regulatory framework could have a material adverse effect on the Company's revenue, results of operations and financial condition.

E-Commerce Law

In addition to laws pertaining specifically to online gaming, Chartwell may become subject to any number of laws and regulations that may be adopted with respect to the Internet and electronic commerce. As well, current laws, which predate or are incompatible with Internet commerce, may be enforced in a manner that restricts the electronic commerce market. The application of such pre-existing Canadian, US and international laws regulating communications or commerce in the context of the Internet and electronic commerce is uncertain.

Moreover, it may take years to determine the extent to which existing laws relating to issues such as intellectual property ownership and infringement, libel and personal privacy are applicable to the Internet.

New laws and regulations that address issues such as user privacy, pricing, online content regulation, taxation, advertising, intellectual property, information security, and the characteristics and quality of online products and services may be enacted.

The adoption of new laws or regulations relating to the Internet, or particular applications or interpretations of existing laws, could decrease the growth in the use of the Internet, decrease the demand for our products and services, increase our cost of doing business or could otherwise have a material adverse affect on the Company's revenue, results of operations and financial condition.

Payment Processing

Commencing in December 2001, certain financial institutions in the US ceased to accept online gaming transactions through their credit cards due to the uncertainty regarding the legality of Internet gaming in the US. This event negatively impacted the online gaming industry as a whole, our licensees and Chartwell. If other financial institutions or credit card issuers in the US or other countries implement similar or additional restrictions, this would have a material adverse effect on the Company's revenue, results of operations and financial condition. This risk has been partially mitigated, however, with Chartwell's ongoing focus on the European market.

Competition

Some of Chartwell's competitors have significantly greater financial, technical, marketing and sales resources and may be able to respond more quickly to changes in customer needs. Additionally, these competitors may be able to devote a greater number of resources to the enhancement, promotion and sale of their games and gaming systems. Our future success is dependent upon our ability to win our share of sales (in the form of new licensees) against these larger competitors. Failure to do so could result in a material adverse effect on the Company's revenue, results of operations and financial condition.

Industry Consolidation

Recently, there has been a significant amount of consolidation in the industry in which we operate. There exists the potential that such consolidation could shrink the list of prospective customers for our services through a rationalization of preferred software vendor suppliers. This factor could have a material adverse effect on the Company's business, revenues, results of operations and financial condition.

Renewal of Software License Agreements

The majority of the Company's revenue is in the form of software license fees. Licensees pay an ongoing fee for the licensing and support of the Company's software under a software licensing agreement, which typically has a three to five year term. The license fee, or royalty, is calculated as a percentage of each licensee's level of activity. There is no assurance that Chartwell will be able to renew agreements with existing clients or that the Company will be able to renew agreements under similar financial and other terms. The failure to renew agreements or the failure to renew agreements under similar financial and other terms could have a material adverse effect on the Company's revenue, results of operations and financial condition.

Dependence on Market Growth

The online gaming market has experienced and is expected to continue to experience significant growth. There can be no assurance that the market for the Company's gaming solutions will continue to grow, that consumers will continue to adapt Chartwell's solutions or that Chartwell will be successful in selling into new and existing markets. If the markets in which our products compete fail to grow, or if the business of the licensees who use our products fails to grow, or grows more slowly than Chartwell currently anticipates, the Company's business, results of operations and financial condition may be materially adversely affected.

Risks Associated with Currency Fluctuations

The majority of Chartwell's revenue is realized in foreign currencies, while the majority of the Company's expenses are incurred in Canadian Dollars. Fluctuations in the exchange rate between the Canadian Dollar and other currencies, particularly the US Dollar and the Euro, may have a material adverse effect on the Company's results of operations and financial condition.

Chargebacks

As a result of increased player deposit levels, our customers are subject to higher exposure to chargebacks, which may also result in possible penalties. Chargebacks are deposit transactions credited to an end user's account that is later reversed or repudiated. This factor could have a material adverse effect on the business of our licensees and accordingly, a material adverse effect on the Company's business, results of operations and financial condition.

Lengthy Sales Cycle

The Company's sales cycle (beginning with an interested customer and culminating in the entering into of a commercial agreement with a customer) typically ranges from six to twelve months and may be longer. This lengthy sales cycle limits Chartwell's ability to forecast the timing of new sales in a specific financial quarter. Any extension in the length of our sales cycle may have a material adverse effect on the Company's revenues and financial condition.

Lengthy Collections Cycle

The Company charges license fees to licensees based on their level of activity. Chartwell's licensees operate in a number of jurisdictions and currencies and are at various stages of maturity and liquidity in their business. As a result of these factors, collections cycles will vary between licensees. A lengthy collections cycle has the effect of increasing the Company's exposure to fluctuations in foreign exchange rates as well as drawing on operating cash flows. Any delay in collections could, therefore, have a material adverse effect on the Company's operating expenses, cash flow and financial condition. As well, the Company's management exercises judgment in making collectibility assumptions on a customer-by-customer basis in determining whether receivables are collectible. Any changes in circumstances may cause these assumptions to be incorrect and could have a material adverse effect on the Company's working capital, net income and financial condition.

Internet Viability and System Infrastructure and Reliability

The growth of Internet usage has caused interruptions and delays in processing and transmitting data over the Internet. There can be no assurance that the Internet infrastructure or the Company's own network systems will continue to be able to support the demands placed on us by the continued growth of the Internet, the overall online gaming industry or that of our customers.

The Internet's viability could be affected by delays in the development or adoption of new standards and protocols to handle increased levels of Internet activity or due to increased government regulation. If critical issues concerning the commercial use of the Internet are not favorably resolved (including security, reliability, cost, ease of use, accessibility and quality of service), if the necessary infrastructure is not sufficient, or if other technologies and technological devices eclipse the Internet as a viable channel, this may negatively affect Internet usage, and our business, revenues, financial condition and operating results will be materially adversely affected.

End-users of our software depend on ISPs, online service providers, gaming site operators and our system infrastructure for access to the sites operated by our licensees. Many of these services have experienced service outages in the past and could experience service outages, delays and other difficulties due to system failures, instability and interruption. Our licensees may lose customers as a result of delays or interruption in service, including delays or interruptions relating to high volumes of traffic or technological problems. As a result, we may not be able to meet the level of service that we have contracted for, and we may be in breach of our contractual commitments, which could have a material adverse effect on the Company's business, revenues, results of operations and financial condition.

Also, the increasing presence of viruses and cyber attacks may affect the viability and infrastructure of the Internet and could materially adversely affect our business.

Security

The Company's Internet gaming software is reliant on technologies and network systems to securely handle transactions and user information over the Internet, which may be vulnerable to system intrusions, unauthorized access or manipulation. As users become increasingly sophisticated and devise new ways to commit fraud, our security and network systems may be tested and subject to attack. There is no assurance that such intrusions or attacks will or can be prevented in the future and any system intrusion or attack may cause a delay, interruption or financial loss, which could have a material adverse effect on our business, results of operations and financial condition.

Reliance on Other Parties

The Company's products rely on ISPs to allow our licensees' customers and servers to communicate with each other. If ISPs experience service interruptions, it would prevent communication over the Internet and would impair our ability to carry on our business.

The ability of our customers to process e-commerce transactions depends on banking processing and credit card systems. Any system failure, including network, software or hardware failure that causes a delay or interruption in e-commerce services could have a material adverse effect on the business of our licensees and accordingly, this could have a material adverse effect on the Company's business, results of operations and financial condition.

Failure to Manage Growth Successfully

The Company's business has grown rapidly in the last four years. The accelerated growth of our business places a strain on managerial and financial resources. This growth, our expansion and the acquisition of Micropower Corporation have resulted in substantial growth to the number of our employees, the scope of our infrastructure and the geographic area of our operations, resulting in increased responsibilities for existing and new management personnel. Our ability to successfully manage this growth depends, in large part, upon our ability to: retain and attract qualified management; retain and attract skilled technical personnel to continue to develop reliable solutions that respond to the evolving needs of our customers; and retain and attract sales and marketing personnel to create an expanding presence in the rapidly growing marketplace for our products. The inability to achieve any of these objectives could harm the Company's business, results of operations and financial condition.

Dependence on Key Personnel

The Company's success is largely dependant upon the performance of its key management, technical and sale personnel. Competition for highly skilled management, technical and sales personnel is intense. The inability to retain and keep employees and to attract and retain additional key employees who have the necessary skills may have a material adverse effect upon the Company's growth and profitability.

Intellectual Property Protection

The Company relies on a combination of laws and contractual provisions to establish and protect our rights in our software and proprietary technology. Our ability to protect our proprietary information is crucial to the success of our business. We do not currently possess any patent or copyright registrations in Canada, the United States or any other jurisdiction. There can be no assurance that the steps we have taken to protect our proprietary rights will be adequate to deter misappropriation of our technology. Any such misappropriation could have a material adverse effect on the Company's business, revenues, results of operations and financial condition.

Similarly, given the nature of the business environment in which we operate, other parties have threatened to issue legal proceedings against the Company based on alleged infringement of intellectual property rights. None of these threats has yet resulted in legal proceedings, however, there can be no assurance that such threats would never materialize into actual litigation or that the Company would prevail in such litigation. An adverse determination in legal proceedings, a costly litigation process or a costly settlement could have a material adverse effect on the Company's business, revenues, results of operation and financial condition.

Proposed Transactions

On August 30, 2006, the Company announced its intention to enter into a business combination with Parlay Entertainment Inc. (“Parlay”) as agreed to in a binding Letter of Intent entered into that same day. The Letter of Intent calls for Chartwell to acquire all of the issued and outstanding common shares of Parlay by way of a plan of arrangement or similar business combination, subject to obtaining all necessary regulatory and court approvals and the approval of the Parlay shareholders and subject to the completion of due diligence by both parties. The definitive agreement to be entered into by Chartwell and Parlay will be subject to a number of conditions, including court approvals, stock exchange approvals and the approval of the shareholders of Parlay at a meeting expected to be held in October 2006. If all necessary approvals are obtained and all other conditions to the completion of the transaction are satisfied or waived, the business combination is expected to be completed by October 31, 2006.

Off Balance Sheet Arrangements

As at the date of this MD&A, the Company has not entered into any off balance sheet arrangements.

Financial Instruments and Other Instruments

The Company does not use financial derivatives or “other financial instruments”.

Other MD&A Requirements

The Company has 18,738,989 common shares outstanding at September 13, 2006. If all of the Company’s options were exercised, the Company would have 20,175,891 common shares outstanding.

The Company’s 2005 Annual Information Form is available on www.sedar.com.