



## ORDER

### III.

On the basis of Respondents' Offers, the Board finds that<sup>1/</sup>:

#### A. Respondents

1. Lawrence Scharfman CPA PA is a public accounting firm located in Boynton Beach, Florida. It is licensed under the laws of the State of Florida to engage in the practice of public accounting (license no. AC0030673). The Firm is registered with the Board pursuant to Section 102 of the Act and PCAOB rules.

2. Lawrence Scharfman, 76, is a certified public accountant who is licensed under the laws of the states of Florida (license no. AC0030673) and New York (license no. 023532-1). At all relevant times, Scharfman was the President and the sole shareholder of the Firm, and an associated person of a registered public accounting firm as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i).

#### B. Summary

3. This matter concerns Respondents' violations of PCAOB rules and auditing standards in auditing the financial statements of Prospero Minerals Corp. ("Prospero"), Cal-Bay International Inc. ("Cal-Bay"), and LitFunding Corp. ("LitFunding"). As detailed below, Respondents failed to perform procedures required by PCAOB auditing standards during the audit of the financial statements of their issuer clients.

4. Respondents violated PCAOB rules and auditing standards in auditing the March 31, 2006 ("FY 2006") and March 31, 2007 ("FY 2007") financial statements of

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<sup>1/</sup> The findings herein are made pursuant to Respondents' Offers and are not binding on any other person or entity in this or any other proceeding. The sanctions that the Board is imposing in this Order may be imposed only if a respondent's conduct meets one of the conditions set out in Section 105(c)(5) of the Act, 15 U.S.C. § 7215(c)(5). The Board finds that Respondents' conduct described in this Order meets the condition set out in Section 105(c)(5)(A), which provides that such sanctions may be imposed in the event of (A) intentional or knowing conduct, including reckless conduct, that results in violation of the applicable statutory, regulatory, or professional standard; or (B) repeated instances of negligent conduct, each resulting in a violation of the applicable statutory, regulatory, or professional standard.

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Prospero. These violations included failing to: (a) plan the audit work; (b) perform sufficient audit procedures on Prospero's largest reported asset; (c) address known material inconsistencies between the other information contained in the FY 2006 10KSB and the financial statements; and (d) assess whether a significant stock issuance was properly valued, disclosed and reported. Respondents also failed to maintain independence from Prospero when, during the course of this engagement, Mr. Scharfman agreed to accept 200,000 shares of company stock.

5. Respondents violated PCAOB rules and auditing standards in their audit of Cal-Bay's 2005 financial statements by: (a) failing to perform sufficient procedures to test the valuation of two assets which, together, constituted more than 90 percent of Cal-Bay's total reported assets; (b) failing to take steps to prevent reliance on their audit opinion after concluding that the previously issued 2005 financial statements were misleading; and (c) adding documents to their work papers after the documentation completion date without complying with PCAOB Auditing Standard No. 3, *Audit Documentation* ("AS3"). The Firm, moreover, failed to take the steps required by Section 10A(b) of the Exchange, after becoming aware that an illegal act had occurred. Mr. Scharfman omitted to take any steps to cause the Firm to comply with Section 10A(b).

6. Respondents violated PCAOB rules and auditing standards in their audit of LitFunding's 2005 and 2006 financial statements by: (a) failing to test the adequacy of a reserve for an asset which constituted 85 percent and 40 percent of LitFunding's 2005 and 2006 total reported assets, respectively; and (b) adding documents to their work papers after the documentation completion date without complying with AS3.

### **C. Respondents Violated Section 10A(b) of the Exchange Act, and PCAOB Rules, Auditing Standards, and Independence Standards**

7. In connection with the preparation or issuance of an audit report, PCAOB rules require that a registered public accounting firm and its associated persons comply with the Board's auditing standards and related professional practice standards.<sup>2/</sup> An auditor may express an unqualified opinion on an issuer's financial statements only when the auditor has formed such an opinion on the basis of an audit performed in

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<sup>2/</sup> See PCAOB Rules 3100, 3200T.

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accordance with PCAOB standards.<sup>3/</sup> Among other things, those standards require that an auditor exercise due professional care, exercise professional skepticism, and obtain sufficient competent evidence to afford a reasonable basis for an opinion regarding the financial statements.<sup>4/</sup> PCAOB rules and standards require associated persons of registered public accounting firms to comply with certain independence restrictions, including restrictions against committing to acquire a financial interest in an audit client.<sup>5/</sup> As detailed below, Respondents failed to meet these standards in connection with the audits of three issuers: the audits of the financial statements of Prospero for FY 2006 and 2007, Cal-Bay for FY 2005, and LitFunding for FY 2005 and 2006. Moreover, Section 10A(b) of the Exchange Act requires firms to take certain steps after becoming aware that an illegal act has taken place. The Firm violated Section 10A(b) in the course of the Cal-Bay engagement. PCAOB Rule 3502 requires that associated persons not omit to take action knowing, or recklessly not knowing, that the omission will directly and substantially contribute to a violation by the firm of the securities laws. Mr. Scharfman violated this rule by failing to cause the Firm to take the steps Section 10A(b) required.

### **Audit of Prospero Minerals Corp.'s 2006 and 2007 Financial Statements**

8. At all relevant times, Prospero was a Nevada corporation based in New York City, NY. Its common stock is registered with the U.S. Securities and Exchange Commission ("Commission") under Section 12(g) of the Exchange Act and is dually quoted on the OTC Bulletin Board and the Pink Sheets. Prospero's public filings disclosed that at all relevant times it was an exploration stage company engaged in the acquisition and development of mineral properties. At all relevant times, Prospero was

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<sup>3/</sup> See AU § 508.07, *Reports on Audited Financial Statements*.

<sup>4/</sup> See AU § 150.02, *Generally Accepted Auditing Standards*; § 230, *Due Professional Care in the Performance of Work*; and § 326, *Evidential Matter*.

<sup>5/</sup> See PCAOB Rules 3100, 3200T (incorporating requirements of certain AICPA auditing standards as in existence on April 16, 2009, including AU § 220, *Independence*), and 3600T (incorporating requirements of certain AICPA independence standards as in existence on April 16, 2003, including ET § 101 and interpretations thereunder).

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an issuer as that term is defined in Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

9. The Firm was engaged as Prospero's auditor beginning on August 14, 2006. During that time, Respondents audited Prospero's 2006 and 2007 financial statements. Respondents issued audit reports dated August 16, 2006 (included in Prospero's Form 10-KSB filed with the Commission on August 17, 2006) and June 22, 2007 (included in Prospero's Form 10-K filed with the Commission on July 27, 2007). Each report stated that the audit was conducted in accordance with the standards of the PCAOB. In each of the audit reports, the Firm expressed an unqualified audit opinion and stated that in the Firm's opinion, Prospero's financial statements presented fairly, in all material respects, Prospero's financial position, results of operations, and cash flows in conformity with Generally Accepted Accounting Principles ("GAAP").

### The 2006 Audit

10. Inquiry of the predecessor auditor is a necessary auditing procedure because it may provide information that will assist the successor auditor in determining whether to accept the engagement, and an auditor should not accept an engagement before evaluating certain communications with the predecessor auditor.<sup>6/</sup> Respondents failed to comply with this standard by accepting the engagement without first inquiring of Prospero's predecessor auditors.

11. Audit work should be adequately planned.<sup>7/</sup> In planning an audit, an auditor should consider the nature, extent, and timing of work to be performed and should prepare a written audit program.<sup>8/</sup> The audit program should set forth in reasonable detail the audit procedures that the auditor believes are necessary to accomplish the objectives of the audit. Respondents failed to comply with this standard. Respondents did not perform or document any planning procedures.

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<sup>6/</sup> See AU § 315.03, .07-.10, *Communications Between Predecessor and Successor Auditors*.

<sup>7/</sup> See AU § 150.02, *Generally Accepted Auditing Standards*; AU § 311, *Planning and Supervision*.

<sup>8/</sup> See AU § 311.05.



Public Company Accounting Oversight Board

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12. Prospero's FY 2006 financial statements reported total assets of approximately \$520,000. Approximately \$425,000, or 80 percent of the assets, was identified as Capital Assets. Respondents failed to perform any procedures to evaluate this significant balance sheet item.

13. In Part I, Item 2 of the FY 2006 Form 10-KSB (the Management Discussion and Analysis section, or "MD&A"), Prospero reported that "on March 31, 2006, Prospero acquired 100% ownership of Lobaye Gold." Prospero reported that this acquisition resulted from an asset purchase agreement "with RCA Resources Corporation ('RCA') for the purchase and sale of all assets of RCA for an acquisition cost of \$64 million," including "a 100% interest in Lobaye Gold SARL" (the "Lobaye Gold acquisition"). Lobaye Gold purportedly was engaged in gold and diamond prospecting in the Central African Republic. Prospero further disclosed that as consideration for this transaction, it issued 80 million shares of company stock to the seller, RCA.

14. The FY 2006 financial statements did not reflect the Lobaye Gold acquisition. While the financial statements did report an \$80,000 increase in the balance of Prospero's outstanding common stock,<sup>9/</sup> they did not reflect the issuance of 80 million shares as disclosed in the MD&A, and earnings per share was calculated based on 9 million outstanding shares.

15. Respondents failed to perform any procedures to assess whether Prospero had appropriately reported and disclosed this acquisition and related stock issuance in Prospero's FY 2006 financial statements. Respondents performed no audit procedures to assess whether the Lobaye Gold assets existed and were valued appropriately. Respondents also performed no procedures to assess whether the company had reasonably valued the 80 million shares issued in exchange for the acquired assets.<sup>10/</sup> Further, the Respondents failed to identify the apparent errors in the

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<sup>9/</sup> The financial statements reported that the par value per share of Prospero's common stock was \$0.001. Thus, an \$80,000 increase in the par value of all outstanding shares, as reported in the financial statements, would reflect the issuance of 80 million shares.

<sup>10/</sup> Based on Prospero's FY 2006 financial statements, the 80 million shares issued in the Lobaye Gold acquisition were assigned a value of \$0.005 per share (\$420,600 of par value and additional paid in capital/80 million shares). During the fiscal quarter in which this transaction closed, however, the low bid and high bid for

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reported number of shares issued as of March 31, 2006 and in the reported loss per common share.

16. Respondents also did not address what they understood to be a material inconsistency between disclosures in Part I, Item 2 and Part II, Item 3.02 of the Form 10KSB, both of which described the Lobaye Gold acquisition as having a cost of \$64 million, and the financial statements, which did not reflect any such acquisition. Respondents were aware of these disclosures and determined that they were materially inconsistent with the financial statements. Respondents should have, but failed to determine whether the financial statements, the audit report, or both required revision.<sup>11/</sup>

17. Respondents also failed to address a potentially material related-party transaction. In Prospero's Form 8-K filed with the Commission on March 20, 2007, Prospero stated that two persons, together, owned almost one-third of the shares of RCA, the seller of the Lobaye Gold assets. Prospero's Forms 10-KSB for FY 2005 and FY 2006 stated that one of these persons was an officer and a shareholder of Prospero, and the other person was a shareholder, officer and director of Prospero at the time of the acquisition. Despite these indications that Prospero insiders stood on both sides of the Lobaye Gold acquisition, Respondents failed to take any steps to determine whether the Lobaye Gold acquisition was a related-party transaction that required specific disclosure in the financial statements.<sup>12/</sup>

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shares of Prospero's common stock were \$1.26 and \$2.15, respectively. Respondents did nothing to assess the reasonableness of the difference between the Company's valuation of the stock issued during the Lobaye Gold acquisition and the trading value of the stock at the time of the acquisition.

<sup>11/</sup> See AU § 550.04, *Other Information in Documents Containing Audited Financial Statements*.

<sup>12/</sup> See AU § 334.11, *Related Parties*.

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### The 2007 Audit

18. In its FY 2007 financial statements, Prospero's Capital Assets increased to \$845,000, and comprised 99.9 percent of the total assets reported as of March 31, 2007. Respondents performed no procedures to test this significant account beyond reconciling the amount reported in the balance sheet to a summary-level worksheet prepared by Prospero.

19. Part II, Item 5 of the FY 2007 Form 10-KSB reported that Prospero acquired all of the assets pertaining to the water purification business of Cavitation Concepts Corporation in exchange for 10 million shares of Prospero's common stock. This transaction increased the reported number of outstanding Prospero common shares from approximately 90 million to approximately 100 million. Respondents failed to perform any procedures to assess whether the assets acquired or the shares issued were fairly valued.

20. Auditor independence is impaired if, during the period of the professional engagement, an auditor had or was committed to acquire any direct or material indirect financial interest in an audit client.<sup>13/</sup> While serving as Prospero's outside auditor, Scharfman committed to acquire 200,000 shares of Prospero stock from a shareholder of Prospero in exchange for services and consultations that Scharfman agreed to perform for the shareholder and for the company. As the auditor with final responsibility for the audit, Scharfman's commitment to acquire a direct financial interest in Prospero impaired his independence.

### **Audit of Cal-Bay's 2005 Financial Statements**

21. At all relevant times, Cal-Bay was a Nevada corporation based in Carlsbad, CA. Its common stock is registered with the Commission under Section 12(g) of the Exchange Act and is dually quoted on the OTC Bulletin Board and the Pink Sheets. Cal-Bay's public filings disclose that it is in the business of acquiring, managing, and selling real estate. At all relevant times, Cal-Bay was an issuer as that term is defined in Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

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<sup>13/</sup> See AU § 220, *Independence*; ET § 101.02, *Independence*.

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22. Respondents were engaged as Cal-Bay's auditors on March 29, 2006. The Firm issued an audit report dated April 12, 2006, which was included in Cal-Bay's Form 10-KSB filed with the Commission on April 17, 2006. In the audit report, the Firm expressed an unqualified audit opinion on Cal-Bay's balance sheet as of December 31, 2005, and the related consolidated statements of operations, changes in "stockholder" (sic) equity" and cash flows for the period ended December 31, 2005. The firm's audit report stated that Cal-Bay's financial statements presented fairly, in all material respects, Cal-Bay's financial position, results of operations, and cash flows in conformity with GAAP. In addition, the Firm's report stated that the audit was conducted in accordance with the standards of the PCAOB.

### Aspen Cove Resort

23. In its 2005 financial statements, Cal-Bay reported that it purchased real estate in Aspen Cove, Utah (the "Aspen Cove Resort"). The financial statements disclosed that Cal-Bay acquired this property by issuing 35 million shares of company stock to the seller, and by assuming an \$800,000 first trust deed against the property. The Aspen Cove Resort constituted approximately 23% percent of the total assets reported in Cal-Bay's 2005 financial statements. Respondents failed to perform adequate audit procedures to test this transaction. Respondents reconciled the reported values to the purchase agreement and reviewed related journal entries, but did nothing to assess whether the acquired asset and shares issued were properly valued.

### West Palm Mortgage Note

24. In its 2005 financial statements Cal-Bay also disclosed that it purchased the first mortgage ("Mortgage Note") position on a parcel of land in West Palm Beach, FL. According to its disclosures, the company purchased the mortgage on the property for \$1,500,000 cash and \$4,000,000 in company stock. Respondents understood that Cal-Bay valued the assets acquired at \$7.8 million, which consisted of \$5.5 million in principal and \$2.3 million of accrued interest.

25. Respondents failed to gather sufficient competent evidential matter to support that the acquired asset was valued appropriately. Furthermore, Respondents failed to address multiple indications that the principal and accrued interest may not be collectible. The Firm's work papers included documents showing that the Mortgage Note was in default, requiring an earlier holder of the note to enter judgment against the mortgagor. Nevertheless, Respondents failed to determine whether any payments had

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been made in settlement of the Mortgage Note. Respondents also failed to perform any procedures to assess whether the value of the land collateralizing the note was sufficient to secure the payment of the Mortgage Note.<sup>14/</sup>

### Cost of Goods Sold

26. Cal-Bay's 2005 financial statements reported a Real Estate Purchase totaling \$1.5 million as Cost of Sales. This amount constituted more than 80 percent of the Cost of Sales reported for 2005. Respondents failed to perform any procedures to determine whether this item was reported appropriately.

### Withdrawal of Audit Opinion

27. PCAOB standards require an auditor who, subsequent to the date of the report upon audited financial statements, becomes aware that facts may have existed at that date which might have affected the report had he or she then been aware of such facts, to take certain steps to address the potential impact of those facts.<sup>15/</sup> When subsequently discovered information is determined to be reliable, to have existed at the date of the report, and would have affected the audit report if the information had been known to the auditor, PCAOB standards require the auditor to advise his client to make appropriate disclosures of the subsequently discovered information and its impact on the financial statements.<sup>16/</sup> If the client refuses to do so, the auditor ultimately is obligated to notify the Commission, among others, that the auditor's report should no longer be relied upon, the nature of the subsequently acquired information, and the information's effect on the financial statements.<sup>17/</sup>

28. After the 2005 Form 10-KSB was filed with the Commission, Respondents determined that Cal-Bay overstated the value of the Mortgage Note. Respondents

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<sup>14/</sup> See AU § 326, *Evidential Matter*.

<sup>15/</sup> See AU § 561, *Subsequent Discovery of Facts Existing at the Date of the Auditor's Report*.

<sup>16/</sup> See AU § 561.06.

<sup>17/</sup> See AU § 561.08b and .09a(i).

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concluded that Cal-Bay should not have recorded as an asset the \$2.3 million of accrued interest due under the Mortgage Note. On April 30, 2006, Respondents requested that Cal-Bay restate its financial statements to remove the \$2.3 million in accrued interest, and informed management that Respondents were withdrawing their opinion on the 2005 financial statements. When Cal-Bay failed to restate its financial results, however, Respondents did not notify the Commission, as PCAOB standards require, that it had withdrawn its audit opinion.

### Failure to Take Required Steps Regarding an Illegal Act

29. The Firm also failed to comply with Section 10A(b) of the Exchange Act. Section 10A(b) requires an auditor to take certain defined steps after detecting or becoming aware that an illegal act has occurred. Likewise, the Firm and Mr. Scharfman violated PCAOB standards, which require auditors to assure themselves that an audit committee or others with equivalent authority at an issuer client are adequately informed with respect to the occurrence of an illegal act.<sup>18/</sup> Scharfman and the Firm were aware that an illegal act had occurred when, in addition to failing to restate its financial results, Cal-Bay also failed to file a Form 8-K disclosing that its auditors had withdrawn their opinion and advised Cal-Bay to restate its financial statements. The Respondents did not thereafter take the steps required by PCAOB standards, and the Firm did not take the steps set forth in Section 10A(b), including reporting its conclusions regarding the likely illegal act to Cal-Bay's Board of Directors. Mr. Scharfman, moreover, violated PCAOB Rule 3502 by omitting to take any action to cause the Firm to follow the steps prescribed in Section 10A(b) knowing, or recklessly not knowing, that such omission would directly and substantially contribute to the Firm's violation of Section 10A(b).

30. Scharfman signed his audit opinion as of April 12, 2006, and the 2005 Form 10-KSB was filed on April 17, 2006. Under AS3, *Audit Documentation*, the documentation completion date would be no later than June 1, 2006 (not more than 45 days after the report release date).<sup>19/</sup> After the documentation completion date, a

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<sup>18/</sup> See AU § 317, *Illegal Acts by Clients*.

<sup>19/</sup> See AS3 at ¶ 15.

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document may be added to an auditor's work papers only if the document indicates the date when it was added, the person who prepared it, and the reason for adding it.<sup>20/</sup>

31. The Firm's work papers include a form audit program released by its publisher in October 2006, months after the documentation completion date. Also, the only copy of the management representation letter contained in the work papers bore a fax header of February 2007, eight months after the latest possible documentation completion date. Scharfman added these documents to his work papers without indicating the date these documents were added, the person who prepared these documents, or the reason for adding these documents.

### **Audits of LitFunding's 2005 and 2006 Financial Statements**

32. At all relevant times, LitFunding Corp. was a Nevada corporation based in Las Vegas, Nevada. Its common stock is registered with the Commission under Section 12(g) of the Exchange Act and is dually quoted on the OTC Bulletin Board and the Pink Sheets. LitFunding's public filings disclosed that at all relevant times it was in the business of investing in litigation recoveries. At all relevant times, LitFunding was an issuer as that term is defined in Section 2(a)(7) of the Act and PCAOB Rule 1001(i)(iii).

33. Respondents were engaged as LitFunding's auditors on April 28, 2006. The Firm issued an audit report dated May 3, 2006, which was included in LitFunding's Form 10-KSB filed with the Commission on May 19, 2006. In the audit report, the Firm expressed an unqualified audit opinion on LitFunding's balance sheet as of December 31, 2005, and the related statements of operations, stockholders equity and cash flows for the period ended December 31, 2005. The Firm's audit report stated that LitFunding's financial statements for the year ended December 31, 2005 presented fairly, in all material respects, LitFunding's financial position, results of operations, and cash flows in conformity with GAAP. In addition, the Firm's audit report stated that the audit was conducted in accordance with the standards of the PCAOB.

34. The Firm also issued an audit report dated May 9, 2007, which was included in LitFunding's Form 10-KSB filed with the Commission on May 14, 2006.<sup>21/</sup> In

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<sup>20/</sup> See AS3 at ¶ 16.

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the audit report, the Firm expressed an unqualified audit opinion on LitFunding's balance sheet as of December 31, 2006, and the related statements of operations, stockholders equity and cash flows for the period ended December 31, 2006. The Firm's audit report stated that LitFunding's financial statements for the year ended December 31, 2006 presented fairly, in all material respects, LitFunding's financial position, results of operations, and cash flows in conformity with GAAP. In addition, the Firm's audit report stated that the audit was conducted in accordance with the standards of the PCAOB.

35. LitFunding's financial statements report that "[c]ontingent advances less reserves for unsuccessful resolution of lawsuits" constituted approximately 85 percent and 40 percent of LitFunding's total reported assets as of December 31, 2005, and December 31, 2006, respectively. In both its 2005 and 2006 financial statements, LitFunding disclosed that management "estimates the net realizable value of contingent advances by periodically reviewing the progress of the cases with the attorneys trying them and past experience with similar cases." The 2005 and 2006 financial statements also disclosed that LitFunding's historical loss rate was 15 percent, before it emerged from bankruptcy, but management calculated its reserve for the unsuccessful resolution of lawsuits using a loss rate of 10 percent, under the assumption that the loss rate would improve following the company's emergence from bankruptcy.

36. Respondents failed to test sufficiently the adequacy of the reserve for the unsuccessful resolution of lawsuits.<sup>22/</sup> Respondents also failed to perform a retrospective review of this significant accounting estimate to determine whether management judgments and assumptions relating to the estimate indicated a possible bias.<sup>23/</sup>

37. In addition, many of the documents included in the Firm's work papers for the 2005 LitFunding audit were added after the documentation completion date, with no

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<sup>21/</sup> LitFunding's original 2006 Form 10-KSB, filed with the Commission on April 18, 2007, failed to include an audit report for the 2006 financial statements.

<sup>22/</sup> See AU § 342, *Auditing Accounting Estimates*.

<sup>23/</sup> See AU § 316.64, *Consideration of Fraud in a Financial Statement Audit*.

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indication of the date these documents were added, the person who prepared these documents, or the reason for adding these documents.<sup>24/</sup>

**IV.**

In view of the foregoing, and to protect the interests of investors and further the public interest in the preparation of informative, fair, and independent audit reports, the Board determines it appropriate to impose the sanctions agreed to in Respondents' Offers. Accordingly, it is hereby ORDERED that:

- A. Pursuant to Section 105(c)(4)(A) of the Act and PCAOB Rule 5300(a)(1), the registration of Lawrence Scharfman CPA PA is revoked; and
- B. Pursuant to Section 105(c)(4)(B) of the Act and PCAOB Rule 5300(a)(2), Lawrence Scharfman is barred from being an associated person of a registered public accounting firm, as that term is defined in Section 2(a)(9) of the Act and PCAOB Rule 1001(p)(i).

ISSUED BY THE BOARD.

/s/ J. Gordon Seymour

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J. Gordon Seymour  
Secretary

August 11, 2009

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<sup>24/</sup> See AS3 at ¶ 16.