SUPREME COURT OF THE UNITED STATES

No. 01–1418

A. ELLIOTT ARCHER, ET UX., PETITIONERS *v.* ARLENE L. WARNER

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT

[March 31, 2003]

JUSTICE BREYER delivered the opinion of the Court.

The Bankruptcy Code provides that a debt shall not be dischargeable in bankruptcy "to the extent" it is "for money . . . obtained by . . . false pretenses, a false representation, or actual fraud." 11 U. S. C. §523(a)(2)(A). Can this language cover a debt embodied in a settlement agreement that settled a creditor's earlier claim "for money . . . obtained by . . . fraud"? In our view, the statute can cover such a debt, and we reverse a lower court judgment to the contrary.

I

This case arises out of circumstances that we outline as follows: (1) *A* sues *B* seeking money that (*A* says) *B* obtained through fraud; (2) the parties settle the lawsuit and release related claims; (3) the settlement agreement does not resolve the issue of fraud, but provides that *B* will pay *A* a fixed sum; (4) *B* does not pay the fixed sum; (5) *B* enters bankruptcy; and (6) *A* claims that *B*'s obligation to pay the fixed settlement sum is nondischargeable because, like the original debt, it is for "money . . . obtained by . . . fraud."

This outline summarizes the following circumstances: In late 1991, Leonard and Arlene Warner bought the Warner Manufacturing Company for $250,000. About six months later they sold the company to Elliott and Carol Archer for $610,000. A few months after that the Archers sued the Warners in North Carolina state court for (among other things) fraud connected with the sale.

In May 1995, the parties settled the lawsuit. The settlement agreement specified that the Warners would pay the Archers "$300,000.00 less legal and accounting expenses" "as compensation for emotional distress/personal injury type damages." App. 61. It added that the Archers would "execute releases to any and all claims . . . arising out of this litigation, except as to amounts set forth in [the] Settlement Agreement." *Id.,* at 63. The Warners paid the Archers $200,000 and executed a promissory note for the remaining $100,000. The Archers executed releases "discharg[ing]" the Warners "from any and every right, claim, or demand" that the Archers "now have or might otherwise hereafter have against" them, "excepting only obligations under" the promissory note and related instruments. *Id.,* at 67; see also *id.,* at 70. The releases, signed by all parties, added that the parties did not "admi[t] any liability or wrongdoing," that the settlement was "the compromise of disputed claims, and that payment [was] not to be construed as an admission of liability." *Id.,* at 67–68, 71. A few days later the Archers voluntarily dismissed the state-court lawsuit with prejudice.

In November 1995, the Warners failed to make the first payment on the $100,000 promissory note. The Archers sued for the payment in state court. The Warners filed for bankruptcy. The Bankruptcy Court ordered liquidation under Chapter 7 of the Bankruptcy Code. And the Archers brought the present claim, asking the Bankruptcy Court to find the $100,000 debt nondischargeable, and to order the Warners to pay the $100,000. Leonard Warner agreed to a consent order holding his debt nondischargeable. Arlene Warner contested nondischargeability. The Archers argued that Arlene Warner's promissory note debt was nondischargeable because it was for "money . . . obtained by . . . fraud."

The Bankruptcy Court, finding the promissory note debt dischargeable, denied the Archers' claim. The District Court affirmed the Bankruptcy Court. And the Court of Appeals for the Fourth Circuit, dividing two to one, affirmed the District Court. 283 F. 3d 230 (2002). The majority reasoned that the settlement agreement, releases, and promissory note had worked a kind of "novation." This novation replaced (1) an original potential debt to the Archers for money obtained by fraud with (2) a new debt. The new debt was not for money obtained by fraud. It was for money promised in a settlement contract. And it was consequently dischargeable in bankruptcy.

We granted the Archers' petition for certiorari, 536 U. S. 938 (2002), because different Circuits have come to different conclusions about this matter, compare *In re West*, 22 F. 3d 775, 778 (CA7 1994) (supporting the novation theory), with *United States* v. *Spicer*, 57 F. 3d 1152, 1155 (CADC 1995) ("The weight of recent authority rejects" the novation theory), cert. denied, 516 U. S. 1043 (1996).

II

We agree with the Court of Appeals and the dissent, *post,* at 1–2 (opinion of THOMAS, J.), that "[t]he settlement agreement and promissory note here, coupled with the broad language of the release, completely addressed and released each and every underlying state law claim." 283 F. 3d, at 237. That agreement left only one relevant debt: a debt for money promised in the settlement agreement itself. To recognize that fact, however, does not end our inquiry. We must decide whether that same debt can *also* amount to a debt for *money obtained by fraud*, within the terms of the nondischargeability statute. Given this Court's precedent, we believe that it can.

Brown v. *Felsen,* 442 U. S. 127 (1979), governs the outcome here. The circumstances there were the following: (1) Brown sued Felsen in state court seeking money that (Brown said) Felsen had obtained through fraud; (2) the state court entered a consent decree embodying a stipulation providing that Felsen would pay Brown a certain amount; (3) neither the decree nor the stipulation indicated the payment was for fraud; (4) Felsen did not pay; (5) Felsen entered bankruptcy; and (6) Brown asked the Bankruptcy Court to look behind the decree and stipulation and to hold that the debt was nondischargeable because it was a debt for money obtained by fraud. *Id.,* at 128–129.

The lower courts had held against Brown. They pointed out that the relevant debt was for money owed pursuant to a consent judgment; they noted that the relevant judgment-related documents did not refer to fraud; they added that the doctrine of res judicata prevented the Bankruptcy Court from looking behind those documents to uncover the nature of the claim that had led to their creation; and they consequently concluded that the relevant debt could not be characterized as one for money obtained by fraud. *Id.,* at 130–131.

This Court unanimously rejected the lower court's reasoning. The Court conceded that the state law of claim preclusion would bar Brown from making any claim "'based on the same cause of action'" that Brown had brought in state court. *Id.,* at 131 (quoting *Montana* v. *United States,* 440 U. S. 147, 153 (1979)). Indeed, this aspect of res judicata would prevent Brown from litigating "all grounds for . . . recovery" previously available to Brown, whether or not Brown had previously "asserted" those grounds in the prior state court "proceeding." 442 U. S., at 131. But all this, the Court held, was beside the point. Claim preclusion did not prevent the Bankruptcy Court from looking beyond the record of the state-court proceeding and the documents that terminated that proceeding (the stipulation and consent judgement) in order to decide whether the debt at issue (namely, the debt embodied in the consent decree and stipulation) was a debt for money obtained by fraud. *Id.,* at 138–139.

As a matter of logic, *Brown*'s holding means that the Fourth Circuit's novation theory cannot be right. The reduction of Brown's state-court fraud claim to a stipulation (embodied in a consent decree) worked the same kind of novation as the "novation" at issue here. (Despite the dissent's suggestions to the contrary, *post,* at 5–6, it did so by an agreement of the parties that would seem to have "sever[ed] the causal relationship," *post,* at 5, between liquidated debt and underlying fraud no more and no less than did the settlement and releases at issue here.) Yet, in *Brown*, this Court held that the Bankruptcy Court should look behind that stipulation to determine whether it reflected settlement of a valid claim for fraud. If the Fourth Circuit's view were correct—if reducing a fraud claim to settlement definitively changed the nature of the debt for dischargeability purposes—the nature of the debt in *Brown* would have changed similarly, thereby rendering the debt dischargeable. This Court's instruction that the Bankruptcy Court could "weigh all the evidence," *id.,* at 138, would have been pointless. There would have been nothing for the Bankruptcy Court to examine.

Moreover, the Court's language in *Brown* strongly favors the Archers' position here. The Court said that "the mere fact that a conscientious creditor has previously reduced his claim to judgment should not bar further inquiry into the true nature of the debt." *Ibid.;* accord, *Grogan* v. *Garner,* 498 U. S. 279, 290 (1991) (assuming that the Bankruptcy Code seeks to "permit exception from discharge of all fraud claims creditors have successfully reduced to judgment"). If we substitute the word "settlement" for the word "judgment," the Court's statement describes this case.

Finally, the Court's basic reasoning in *Brown* applies here. The Court pointed out that the Bankruptcy Code's nondischargeability provision had originally covered "only 'judgments' sounding in fraud." 442 U. S., at 138. Congress later changed the language so that it covered all such "'liabilities.'" *Ibid.* This change indicated that "Congress intended the fullest possible inquiry" to ensure that "all debts arising out of" fraud are "excepted from discharge," no matter what their form. *Ibid.;* see also 11 U. S. C. §523(a) (current "any debt" language). Congress also intended to allow the relevant determination (whether a debt arises out of fraud) to take place in bankruptcy court, not to force it to occur earlier in state court at a time when nondischargeability concerns "are not directly in issue and neither party has a full incentive to litigate them." *Brown*, 442 U. S., at 134.

The only difference we can find between *Brown* and the present case consists of the fact that the relevant debt here is embodied in a settlement, not in a stipulation and consent judgment. But we do not see how that difference could prove determinative. The dischargeability provision applies to all debts that "aris[e] out of" fraud. *Id.,* at 138; see also *Cohen* v. *de la Cruz,* 523 U. S. 213, 215 (1998). A debt embodied in the settlement of a fraud case "arises" no less "out of" the underlying fraud than a debt embodied in a stipulation and consent decree. Policies that favor the settlement of disputes, like those that favor "repose," are neither any more nor any less at issue here than in *Brown*. See 442 U. S., at 133–135. In *Brown*, the doctrine of res judicata itself ensured "a blanket release" of the underlying claim of fraud, just as the contractual releases did here, *post,* at 2–3. See *supra,* at 4. Despite the dissent's protests to the contrary, *post,* at 1–3, what has *not* been established here, as in *Brown,* is that the parties meant to resolve the *issue* of fraud or, more narrowly, to resolve that issue for purposes of a later claim of nondischargeability in bankruptcy. In a word, we can find no significant difference between *Brown* and the case now before us.

Arlene Warner argues that we should affirm the Court of Appeals' decision on alternative grounds. She says that the settlement agreement and releases not only worked a novation by converting potential tort liabilities into a contract debt, but also included a promise that the Archers would not make the present claim of nondischargeability for fraud. She adds that, in any event, because the Archers dismissed the original fraud action with prejudice, North Carolina law treats the fraud issue as having been litigated and determined in her favor, thereby barring the Archers from making their present claim on grounds of collateral estoppel. But cf. *Arizona* v. *California,* 530 U. S. 392, 414 (2000) ("[S]ettlements ordinarily occasion no *issue preclusion* . . . unless it is clear . . . that the parties intend their agreement to have such an effect").

Without suggesting that these additional arguments are meritorious, we note that the Court of Appeals did not determine the merits of either argument, both of which are, in any event, outside the scope of the question presented and insufficiently addressed below. See *Roberts* v. *Galen of Va., Inc.,* 525 U. S. 249, 253–254 (1999) *(per curiam).* We choose to leave initial evaluation of these arguments to "[t]he federal judges who deal regularly with questions of state law in their respective districts and circuits," and who "are in a better position than we," *Butner* v. *United States,* 440 U. S. 48, 58 (1979), to determine, for example, whether the parties intended their agreement and dismissal to have issue-preclusive, as well as claim-preclusive, effect, and to what extent such preclusion applies to enforcement of a debt specifically excepted from the releases, *supra*, at 2; *post*, at 3. The Court of Appeals remains free, on remand, to determine whether such questions were properly raised or preserved, and, if so, to decide them.

We conclude that the Archers' settlement agreement and releases may have worked a kind of novation, but that fact does not bar the Archers from showing that the settlement debt arose out of "false pretences, a false representation, or actual fraud," and consequently is nondischargeable, 11 U. S. C. §523(a)(2)(A). We reverse the Court of Appeals' judgment to the contrary. And we remand this case for further proceedings consistent with this opinion.

It is so ordered.